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**The Ties that Bind: Big Business and Center-Periphery Relations in  
the Russian Federation**

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**The Ties that Bind: Big Business and Center-Periphery Relations in  
the Russian Federation**

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## **Dedication**

For Irina

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# **The Ties that Bind: Big Business and Center-Periphery Relations in the Russian Federation**

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This dissertation examines the development of Russian federalism from 1990-2002, focusing on patterns of intergovernmental conflict and cooperation that have persisted across both the Yeltsin and Putin presidencies. It argues that unexpected instances of cooperation between the federal government and the wealthier regions can be explained by the political and economic integrating role of Russia's largest business actors, or "national-level" businesses. As these businesses increase their impact on regional political economies, they tend to enhance the central government's capacity to coerce and co-opt regional politicians. Although the comparative politics literature has increasingly emphasized the dangers of political decentralization in democratizing federal states, this study demonstrates how certain types of state-business alliances can, instead,

bind the interests of federal and regional politicians, helping to “make federalism work” in an environment of intense economic adjustment and weak democratic institutions.

The dissertation concludes with an assessment of two contrasting scenarios focused on the direction of Russia’s federal system during the next several years. One scenario is clearly more positive than the other, envisioning the gradual institutionalization of the state-business relationship, coupled with the development of a strong national party system, as contributing to a deepening of democratic federalism and to a “market-preserving” balance of power in intergovernmental relations that would promote economically salutary competition between subnational governments. The other, more negative, scenario foresees national-level businesses as becoming instruments of coercive recentralization in Russia’s federal system, with potentially deleterious effects for democratic consolidation and fiscal federal performance.



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## **Introduction**

What makes federalism work? Renewed interest in the dynamics of federal systems and their consequences for political stability, democratic consolidation and economic performance has heightened greatly since the third wave of democratization crested a decade ago. For the Russian Federation, which encompasses eleven different time zones, 89 sub-national regions and dozens of ethnic groups, finding a democratic solution to the numerous, multifaceted problems of federal governance has been a pressing issue. Throughout the 1990s, Russia's center-periphery relations involved both conflict and accommodation between the Kremlin and an array of recalcitrant regional governments that championed their own fiscal and political autonomy. Moscow's inability to control the pace of decentralization produced an unstable and asymmetrical federal arrangement, in which the federal government had limited capacity to implement coherent policies and establish a uniform market and rule of law.

Although Russia managed to avoid the ultimate fate of its Soviet successor state and ethnofederal neighbors in Eastern Europe, such as Czechoslovakia, lingering regional defiance has continued to frustrate President Putin's attempts to re-establish federal preeminence and enforce mandates uniformly. Understanding the factors that both drive and constrain aggressive regional behavior in federal systems is essential for the study of democratization in large countries generally. For Russia in particular, it is important to understand how the centrifugal forces unleashed by its dual economic and political transition can be managed without backsliding toward the Soviet past.

This study developed in response to a puzzle. In the comparative politics literature, natural resource wealth and industrial development have traditionally been associated with higher levels of assertive, autonomy-seeking behavior by regions toward the federal center, such as demands for state restructuring and expansion of control over fiscal and political resources. The opportunities for such behavior can be even greater in periods of political openings, intense economic adjustment and increased exposure to global markets, all of which have been evident in the Russian case. Yet, Russia's wealthiest regions – the “winners” of the market transition – are clearly divided into two distinct groups, “assertive” and “loyal.” Consistent with the conventional wisdom, the first of these two sets of regions has pursued assertive strategies, including disruptive acts of political and economic separatism under Yeltsin, as well as overt resistance to Putin's attempts to harmonize federal and regional legislation and phase out the special deals contained in bilateral power-sharing agreements signed under his predecessor. On the other hand, the second set of regions has far more often followed strategies of loyalty and cooperation with the federal center, exhibiting both greater restraint in the public political arena under Yeltsin, and more readily acquiescing to the recentralization of authority under Putin.

While political resource mobilization opportunities inherited from the Soviet Union's ethnofederal structure can explain part of this dichotomous pattern, they cannot account for the divergence of behavior within subsets of ethnic and non-ethnic regions, which are found in both the “assertive” and “loyal” categories. Neither does the nature of Russia's fiscal federal arrangement fully answer this question, for many of the clearly

“loyal” regions possess high levels of bargaining power with Moscow as net contributors to the federal budget. Moreover, the relative difference in regional behavior has remained consistent over the past decade despite the redesign of federal institutions, the strengthening of the executive apparatus, and a sharp change in national leadership.

I argue that unexpected instances of cooperation between the federal government and the wealthier regions can be explained by the political and economic integrating role of Russia’s largest business actors, or “national-level” businesses. The top echelon of businesses in Russia is a natural ally of the federal center, and has enhanced its capacity to both coerce and co-opt elites in the wealthier regions where these businesses have a strategic interest. I develop a theoretical framework for viewing national-level businesses as both “sticks” and “carrots” that can reduce the economic incentives and political opportunities for regional politicians to engage in confrontational behavior vis-à-vis Moscow. I then employ both quantitative and qualitative methods to show that higher degrees of “penetration” by national-level business actors in regional political economies result in lower levels of assertiveness by these regions in the federal bargaining game.

Various scholars have emphasized the perverse incentives that federal institutions can create for regional politicians in democratizing and emerging-market countries to undermine public goods such as national political and fiscal stability in their pursuit of particularistic interests. In the Russian case, alliances between powerful, rent-seeking enterprises and their political patrons in regional governments have been customarily viewed as exacerbating this potential danger associated with federal systems. This study demonstrates how certain types of state-business alliances have actually contributed to

the stability of Russia's federal system over the last decade. In particular, I focus on the relative size and structure of big businesses. By forging alliances with both federal politicians and officials in regions where their production assets are located, Russia's largest, vertically-integrated businesses have served as a tie that binds the post-Soviet federal state in the context of weak national party penetration in the periphery.

The capacity of national-level businesses to act as mechanisms of political integration reflects a different side of state-business relations than that customarily found in the literature on "oligarchic capitalism" in Russia. It is true that the business oligarchy that emerged from Russia's mass privatization program in the early nineties has been blamed for capturing the state and resisting further progress in economic reform in order to defend its initial gains. Yet, even though politically powerful business actors have had a "horizontally" fragmenting effect on the federal government by dividing the loyalties of public officials among competing financial-industrial groups, they have also played a "vertically" integrating role in Russia's federal system. The acquisition of enterprises in key sectors of Russia's economy by national-level businesses has facilitated the construction of economic hierarchies that have supplemented political ones.

The fact that the Russian Federation began its democratic transition as a weak state in the midst of a relatively chaotic process of decentralization, but is now more clearly headed toward greater centralization makes it an intriguing case for gauging the effect of business actors on center-periphery relations. No matter what road Russia takes politically, the need to integrate into the global economy will make a complete retreat toward the Soviet command-administrative model unlikely. In order to harness the full



economic potential of sub national competition in Russia's federal state, the Kremlin must balance centralization with a measure of political and fiscal autonomy for regional governments. In addition to a strong formal state hierarchy, this requires various integrating mechanisms to structure bargaining and reciprocity among federal and regional politicians. The dissertation establishes a framework for viewing national-level businesses, with their considerable political and economic resources, as playing an important role in maintaining this balance and "making federalism work."

### **STRUCTURE OF THE DISSERTATION**

The first chapter of the dissertation offers a review of the comparative literature on the divergent experiences of democratizing states over the past two decades, which have shown that federal systems can be a double-edged sword, enhancing or undercutting political stability, democratic consolidation and public sector performance. After reviewing critiques of Russian federalism, the chapter examines the dynamics of intergovernmental bargaining and the variables commonly employed in the literature to explain how regions in federal systems behave. Two sets of variables are highlighted, including "demand-side" ones, which include economic incentives and political bargaining power, and also political-institutional constraints, which include the durability and fairness of the "federal bargain", the strength of the state bureaucracy and national party system, as well as national leadership and changing patterns of federal responses to regional assertiveness. These variables are then examined in the context of both the Yeltsin and Putin presidencies. The chapter concludes with the contention that

conventional understandings of federalism do not adequately explain variations in regional behavior in Russia.

Chapter 2 develops a theoretical perspective for explaining the divergence in the behavior of Russia's wealthier regions. It makes the case for incorporating a missing variable – the relative influence of national-level businesses in the wealthy regions. The various forms of political and financial influence, or “carrots” and “sticks,” that national-level business can use to influence regional strategies in the federal bargaining game are outlined. The chapter concludes by presenting a triangular view of federal system dynamics that captures the interconnectedness between big business actors and regional and federal governments in the Russian case.

Chapter 3 provides a closer look at the dynamics of intergovernmental relations throughout the Russian transition toward democracy, dividing Russian federalism from 1990-2002 into three phases, and highlighting the change and continuity in both regional agendas and the formal and informal rules of the federal bargaining game. While political opportunism certainly has been a motivating factor for regional assertion, especially in the earlier years of the transition and by Russia's “ethnic republics,” the strains of economic adjustment have been a common denominator impelling aggressive regional strategies in the intergovernmental arena. Moreover, patterns of accommodation and reciprocity during federal election cycles have been a thread that has stretched across intergovernmental relations during both the Yeltsin and Putin presidencies.

Chapter 4 provides statistical evidence that national-level businesses have helped to structure more cooperative patterns of center-periphery relations. It begins by identifying the

“national-level” subset of Russian businesses, and then overviews the institutional context that has amplified their political role in Russia’s federal system. Several versions of multivariate regression analysis are presented to demonstrate the statistical relationship between the level of “penetration” of national-level business actors in the wealthy regions’ political economies and these regions’ level of assertiveness in the federal bargaining game. Dividing the dependent variable, or regional assertiveness index, across time also shows that the various waves of national-level business expansion have increasingly structured center-periphery relations in Russia.

Chapter 5 suggests a way of categorizing the wealthy regions through the prism of the dissertation's political economy framework. It begins by identifying three typologies of regions: consistently loyal, consistently assertive and those regions demonstrating declining assertiveness. It then reviews the two “waves” of national-level business expansion into the periphery under Presidents Yeltsin and Putin, respectively. Regions that were able to limit the expansion of national-level business actors into their jurisdictions during both of these waves have been the most consistently assertive. By contrast, in regions where national-level businesses have maintained a strategic presence since the early 1990s, pressing jurisdictional and distributional issues have generally been resolved via power-sharing settlements between these businesses and the regional administrations, in place of more risky strategies of assertion toward Moscow. Finally, the third category of regions initially pursued assertive strategies in the federal bargaining game, but then became “quieter” after national-level businesses expanded into their territories beginning in 1999.

The sixth and concluding chapter examines the empirical and normative implications of the study. In particular, it emphasizes the role of big business as a “balancing” mechanism in Russia’s federal system. It makes the case that the evolving nature of the state-business relationship is important for Russia’s prospects of achieving democratic federalism, as well as a “market-preserving” balance in intergovernmental relations that would promote efficiency-enhancing interregional competition. The chapter concludes with an assessment of two contrasting scenarios about the direction of Russia’s federal system during the next several years.

## **Chapter 1: Russian Federalism in the Comparative Perspective**

The tumultuous and conflict-ridden 1990s demonstrated the dangers inherent in federal systems throughout Eastern Europe and the post-Soviet region. In the Russian case, assertive, autonomy-seeking strategies adopted by regional elites undermined the central government's capacity to effectively coordinate decentralization, leading to ethnic conflict, macroeconomic instability, and ultimately threatening state breakdown.

Although the immediate threat of territorial disintegration has since subsided, instances of regional defiance, most notably and violently by Chechnya, continue to frustrate the Kremlin's efforts to reestablish a strong central state able to effectively govern.

Understanding the factors that both drive and limit regional assertiveness in federal systems is important, because Russia must still cope with the challenge of managing the centrifugal forces unleashed by political decentralization, ethno nationalism and integration into the global economy.

This chapter presents a framework for analyzing the dynamics of regional assertiveness in federal systems. It begins by reviewing the comparative and Russian area literature on federalism, focusing on the effects that federal institutional arrangements have on political and economic performance in democratizing countries. Concluding that Russian federalism has failed to live up to its full potential thus far, it asks an important question for large democratizing states: what makes federalism work?

The second part of the chapter addresses this question by offering an overview of the dynamics of elite bargaining in federal systems. After outlining various types of

federal outcomes that result from the interaction of federal and regional strategies, it then narrows the question to explaining patterns of regional behavior: why were some regions consistently assertive, while others demonstrated greater constraint during both the Yeltsin and Putin presidencies?

The third section reviews the traditional variable set used in the literature to explain regional behavior in federal systems. Two sets of factors are highlighted: economic and ethnicity-based drivers on one hand, and political and institutional constraints on the other. I conclude by arguing that the conventional wisdom does not adequately explain the variation in regional behavior in the Russian case, especially within the cohorts of ethnic and non-ethnic regions. These observations provide the foundation for the dissertation's thesis pursued in Chapter 2.

## **FEDERALISM AND ITS CRITICS**

### **The logic of balance**

As Watts's notes, the term "federalism" is applied to a wide range of institutional arrangements in the comparative literature. Included under the umbrella of federalism are federal political systems, which are broadly characterized by a combination of "shared-rule and self-rule," and the more narrow set of federations, distinguished by the constitutional division of rights and responsibilities within a multi-tiered government where each level is held responsible by direct elections.<sup>1</sup> Riker's definition perhaps best addresses the central feature of federalism: "a political organization in which the

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<sup>1</sup> Watts defines federal systems as "a genus of political organization that is marked by the combination of shared-rule and self-rule." Federations are a subspecies of federal systems: "a compound polity combining constituent units and a general government, each possessing powers delegated to it by the people through a

activities of government are divided between regional and central governments in such a way that each kind of government has some activities on which it makes final decisions.”<sup>2</sup> Indeed, the importance of guaranteed autonomous spheres of decision-making authority in certain policy arenas is central to the idea of federalism.<sup>3</sup> In this sense, it is just as much designed to keep levels of government at an arms-length distance from each other as it is to foster intergovernmental cooperation and accommodation.<sup>4</sup>

It could be argued that this concept of balance is perhaps the distinguishing feature of federal systems, since there is no set blueprint for political institutions, nor is there a specific threshold for the level of fiscal or policy decentralization.<sup>5</sup> Indeed, Smith labels federal systems as "decentered," noting that federalism has been represented as both "centralizing and decentralizing ideolog[ies] as well as a doctrine of balance.”<sup>6</sup> Likewise, Elazar refers to federal systems as being "non-centralized.”<sup>7</sup> In this context, federalism is a point on a spectrum somewhere midway between a confederal system, where the constituent units could routinely override any decision of the central government (such as happened in the Soviet Union during its final years of existence),

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constitution, each empowered to deal directly with the citizens in the exercise of a significant portion of its legislative, administrative, and taxing power, and each directly elected by its citizens”(121). Ronald Watts, “Federalism, Federal Political Systems, and Federations,” *Annual Review of Political Science* 1: (1998) 117-37.

<sup>2</sup> William Riker, “Federalism” in *Government Institutions and Processes*, Fred Greenstein and Nelson Polsby, eds. (Reading, Mass: Addison-Wesley, 1975).

<sup>3</sup> Riker, *Federalism: Origin, Operation and Significance* (Boston: Little Brown, 1964). Usually, the “federal guarantee” is a statement in the constitution proclaiming federal power-sharing principles.

<sup>4</sup> Richard Deeg, “Economic Globalization and the Shifting Boundaries of German Federalism,” *Publius: The Journal of Federalism*, 26:1 (Winter 1996), 27-52.

<sup>5</sup> See, for instance, Ronald Watts, *Comparing Federal Systems* (Montreal and Kingston: McGill-Queen’s University Press, 1999) on the variety of federal systems and the complexity of cross-national comparison.

<sup>6</sup> Graham Smith, “Introduction,” in *Federalism: the Multiethnic Challenge* (London, New York: Longman, 1995).

<sup>7</sup> Daniel Elazar, *Exploring Federalism* (Tuscaloosa, AL: University of Alabama Press, 1987).

and a unitary system, where there are no formal safeguards against the central government arbitrarily revoking authority that has been devolved, regardless of the de-facto level of fiscal or policy-making decentralization. As a decentralized unitary state, China would currently be an example of the latter case.

### **Federalism: panacea or pitfall?**

In larger and geographically diverse countries transitioning from authoritarian rule, federal institutional arrangements can be used as a means of constitutionally preserving certain spheres of regional and local autonomy against the threat of encroachment by the central government.<sup>8</sup> A distinguishing feature of federations (as a sub-species of federal systems) is the greater level of political decentralization enshrined in the constitution and secured by sub-federal elections.<sup>9</sup> In particular, local elections can increase the quality and legitimacy of democracy by enhancing local government responsiveness and increasing citizen participation, which is especially important in countries with ethnically heterogeneous populations.<sup>10</sup> Security against unilateral revisions to a region's status is particularly important for co-opting minority groups which might otherwise resort to secession or conflict.<sup>11</sup> Furthermore, in presidential

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<sup>8</sup> An independent judiciary is important component of maintaining cooperative resolution of intergovernmental disputes.

<sup>9</sup> In most federations, jurisdictional rules – which demarcate the division of political authority and autonomous spheres of policy discretion among levels of government – are embedded in the constitution, while distributional (e.g. fiscal federal) rules are enumerated in federal legislation and various types of intergovernmental agreements that are generally subject to continuous negotiation by officials. See Mark Krasnick ed. *Fiscal Federalism* (Toronto: University of Toronto Press, 1986), especially the chapter by Anthony F. Sheppard, “Taxation Policy and the Canadian Economic Union.”

<sup>10</sup> Larry Diamond, *Developing Democracy: Towards Consolidation* (Baltimore: John Hopkins University Press, 1999).

<sup>11</sup> See, for instance, Donald L. Horowitz, *Ethnic Groups in Conflict* (Berkeley: University of California Press, 1985). See also T. Gurr, *Minorities at Risk: A Global View of Ethnopolitical Conflicts* (Washington,



systems, federalism serves to mitigate the “winner take all” aspect of national elections: by electing governors in key regions, an opposition party can gain access to state resources, influence policy outcomes and participate in governance via federalism’s interwoven political arenas.<sup>12</sup>

Finally, according to fiscal federal theory, the benefits of federalism are enhanced when accompanied by a measure of economic decentralization.<sup>13</sup> The devolution of fiscal authority and responsibility to subnational governments can improve local service delivery and lead to greater experimentation and innovation. In developing countries in particular, properly functioning federal institutions shield markets from government interference while at the same time promoting salutary subnational competition to attract capital and labor.<sup>14</sup>

Not all scholars are convinced that federalism is inherently beneficial, however, especially for newly democratizing countries. In comparison with unitary systems, subnational elites in federations have greater opportunities to mobilize political and fiscal resources in pursuit of their own particularistic agendas.<sup>15</sup> The federal government is responsible for the public good – policies that benefit the federation as a whole – while

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DC: U.S. Institute of Peace, 1993), and Arend Lijphart, *Democracy in Plural Societies* (New Haven: Yale University Press, 1977).

<sup>12</sup> Joanne Brzinski, "Changing Forms of Federalism and Party Electoral Strategies: Belgium and the European Union," *Publius: The Journal of Federalism*, Winter 1999, v.29, 1, 45.

<sup>13</sup> Wallace Oates, *Fiscal Federalism* (New York: Harcourt, Brace, Jovanovich, 1972), 3-20.

<sup>14</sup> Richard Bird and Francois Vaillancourt eds., *Fiscal Decentralization in Developing Countries* (Cambridge, New York: Cambridge University Press, 1999).

<sup>15</sup> See for instance Alfred Stepan, “Russian Federalism in the Comparative Perspective,” *Post-Soviet Affairs*, 16(2):2000, 133-176.

sub-federal elites are beholden to geographically particular constituencies.<sup>16</sup> If left unchecked, rent-seeking behavior "from below" may undermine national public goods such as policy standardization and market regulation, as well as economic growth and political stability.<sup>17</sup>

In transitional countries, where democratic accountability may be generally weaker, elections at the sub-federal level have as much potential to do harm as good. As old channels of vertical accountability are severed and the power bases of regional politicians become less dependent on national level decision-makers, the federal center's ability to punish potentially destabilizing behavior, such as fiscal irresponsibility, autarky and political assertiveness, decreases. Thus, if the local decision-making process is not democratic, decentralization will lead to less manageable and less accountable regional government.<sup>18</sup>

Even in developed democratic federations, the overlapping of federal and regional jurisdictions inherent in multi-tiered government generates incentives for jurisdictional and distributional conflict, while federalism's multiple veto points can fragment the policy process.<sup>19</sup> Moreover, the additional venues for electoral politics provided by sub-federal elections can lead to a more geographically fragmented party system, which is

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<sup>16</sup> A good overview of the literature on the collective action problem in federal systems can be found in Erik Wibbles, "Federalism and the Politics of Macroeconomic Policy and Performance," *American Journal of Political Science* 44:10 (2000): 687-702. Regional politicians have an incentive to free-ride on public goods such as national macroeconomic stability while trying to carve off the largest piece of the federal pie for themselves. In the absence of strong market discipline and central political coordination, this can lead to poor fiscal performance and crises.

<sup>17</sup> Ibid. The Russian-area literature also echoes this view, as demonstrated below.

<sup>18</sup> Remy Prude'homme, "The Dangers of Decentralization," *World Bank Research Observer*, 10, no.2, (August 1995): 201-20.

<sup>19</sup> One school of critique can be found in the historical-institutionalist literature. See, for instance, David Robertson and Dennis Judd, *The Development of American Public Policy: the Structure of Policy Constraint* (Glenview: Scott, Foresman and Company, 1989).

especially true when federalism emerges via decentralization, as in the case of Russia, rather than centralization, as in the case of the US and, more recently, the EU.<sup>20</sup>

As several studies have shown, the regionalization of politics is even starker during the initial period of democratization. Perhaps the greatest failure of federalism is reflected in the wave of state disintegration in the nineties. Based on the experiences of the Soviet Union, Czechoslovakia and Yugoslavia, various scholars have warned of the dangers of ethnofederal systems during periods of political openings and decentralization.<sup>21</sup> In these countries, the legacy of federal institutions provided resources (administrative levers, symbolic trappings of statehood) for regional elites to create alternative political identities and mobilize the population against the center. While federal institutions may be harmless when ethnic identity is latent, they can play a "subversive" role at times of political openings when the center attempts to broaden political participation.<sup>22</sup>

While ethnofederal systems may be more prone to political instability than unitary countries during transitions, research has also shown that emerging market federations are more susceptible to macro-economic crises. In general, emerging market countries lack a sophisticated market infrastructure to enforce responsible fiscal behavior at the

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<sup>20</sup> Joanne Brzinski, "Changing Forms of Federalism and Party Electoral Strategies: Belgium and the European Union," *Publius: The Journal of Federalism*, Winter 1999, v.29, 1, 45; Mark Jones, "Federalism and the Number of Parties in Argentine Congressional Elections," *The Journal of Politics*, Vol 59, No.2, May 1997, 538-49; Herman Bakvis and William Chandler, *Federalism and the Role of the State* (Toronto, Buffalo, N.Y.: University of Toronto Press, 1987).

<sup>21</sup> Carol Leff, "Democratization and Disintegration in Multinational States," *World Politics*, 51:2, 1999, 205-235; Valerie Bunce, *Subversive Institutions: the Design and the Destruction of Socialism and the State* (Cambridge/New York: Cambridge University Press, 1999); and Mark Beissenger, *Nationalist Mobilization and the Collapse of the Soviet State* (New York: Cambridge University Press, 2002).

<sup>22</sup> Bunce, 1999.

regional level. Instead of reaping the salutary economic benefits of fiscal federal (e.g. interregional) competition, many emerging market federations have suffered from what Wibbles has labeled “political federalism,” or rent-seeking by regional politicians, which undermines national fiscal performance.<sup>23</sup>

That federal systems account for one factor explaining the divergence in progress toward market reform among third-wave countries (especially between Eastern Europe and the former Soviet Union, which had similar starting points) has prompted scholars to focus on the sequencing of reforms in democratizing federations, and to suggest that economic reform proceed political decentralization.<sup>24</sup> This in turn is tied into the larger question of central state capacity during transitions. For instance, various comparisons between China and Russia have highlighted the importance of the balance between regional autonomy and the capacity of the central state; the latter must be strong enough to deter rent-seeking behavior, while properly regulating fiscal federal competition, which entails maintaining a unified national market space.<sup>25</sup> Inheriting a weak central state unable to hold regional leaders politically accountable is therefore another condition that can exacerbate the “subversive” effects of federal systems.

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<sup>23</sup> See Wibbles, “Federalism and the Politics of Macroeconomic Policy and Performance,” 2000. Federal systems provide regional leaders with an incentive to maximize resources within their jurisdictions, and free ride in regard to public goods such as a stable currency, which is solely the responsibility of the federal government.

<sup>24</sup> Treisman, Daniel. “Political Decentralization and Economic Reform: A Game-Theoretic Analysis,” *American Journal of Political Science*, 43, 2 (April 1999): 448-517.

<sup>25</sup> Oliver Blanchard and Andrey Schleifer, *Federalism With and Without Political Centralization: China versus Russia*. NBER Working Paper Series, Cambridge, MA: National Bureau of Economic Research, 2000; and Darrell Slider “Russia’s Market-Distorting Federalism.” *Post-Soviet Geography and Economics*, 38 (October, 1997): 445-460.

By all accounts, in the early nineties the Russian Federation fitted the profile of a "risk case" for political decentralization according to the comparative literature: an ethnofederal system inherited from the Soviet Union, undeveloped democratic and market institutions (emerging-market federation), and a massive economic reform agenda accompanied by a crisis in the real economy that exacerbated distributive conflict. The central state at the time of transition in 1991 was also on the verge of a constitutional crisis, and severe executive-legislative tensions reduced its capacity to attend to problems in the periphery. Not only was the transition legacy stacked against the Russian government, but as Barany and Moser note, the choices made by key policy makers in the early transition period also restricted the government's ability to build effective political and market institutions throughout the first decade of the transition.<sup>26</sup>

### **Russian Federalism: a failed experiment?**

Given this array of challenges, it is not surprising that throughout the 1990s the contours of center-periphery relations in Russia were shaped by waves of conflict and accommodation between the Kremlin and recalcitrant regional governments championing fiscal and political autonomy. Moscow's inability to impose uniform rules on the regions and control the pace of political decentralization resulted in an unstable and asymmetrical federal arrangement, undermining the federal government's capacity to implement coherent national policy objectives and establish a uniform market space and rule of

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<sup>26</sup> "Introduction" in Zoltan Barany and Robert Moser, eds. *Russian Politics: Challenges of Democratization* (Cambridge, New York: Cambridge University Press, 2001).

law.<sup>27</sup> Indeed, under Yeltsin the Russian federal system increasingly lurched toward the confederal end of the spectrum in terms of regional assertiveness and central state weakness, which prompted some observers to view the situation as nearing state breakdown as local autarky intensified in the latter part of the nineties.<sup>28</sup>

Even though the larger threat of instability and conflict had subsided by the time President Putin began his first term in 2000 – with the exception of the breakaway republic of Chechnya – various cases of regional defiance have continued to frustrate the Kremlin's attempt to re-establish federal preeminence and enforce mandates to dismantle the asymmetrical federal system forged during the nineties. Indeed, despite a much more impressive arsenal of formal-legal “sticks,” during Putin's first term the Kremlin was forced in large measure to continue a Yeltsin-era pattern of individual bargaining with recalcitrant executives.<sup>29</sup>

While there is certainly no question that some degree of recentralization was necessary after the “federalism” that had emerged in the late nineties, the danger is that eventually the pendulum might swing too far in the opposite direction during Putin's second term, and that a more or less de-facto unitary system might emerge. In addition to backtracking in democratic consolidation, strictly “top-down” governance – in the context of Putin's so-called managed democracy – could also stifle the economic benefits of fiscal federalism.<sup>30</sup>

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<sup>27</sup> Stoner-Weiss, 1999 and Slider, 1997.

<sup>28</sup> Gail Lapidus, “Asymmetrical Federalism and State Breakdown in Russia,” *Post Soviet Affairs*, 15 (January), 1999: 74-82.

<sup>29</sup> Daniel Treisman, “How Different is Putin’s Russia?” *Foreign Affairs* 81:6 (2002).

<sup>30</sup> One of the conditions for “market-preserving” federalism in transitional states is that one level of government cannot unilaterally change the rules without the consent of the other. Barry Weingast, “The

Based on this brief overview, it is clear that federal relations have been, and continue to be, problematic in terms of overall political stability, democratic consolidation and economic performance. Inasmuch as federalism represents an ideology of balance, or a middle road between a loosely knit, confederal-type system, which is where Russia seemed to be headed under Yeltsin, and de-facto unitary relations, which seems to be a potential direction now under Putin, the major question that arises is “what makes federalism work?” In other words, how can Russia avoid the dangers of decentralization without trading off the benefits of democratic federal governance? Answering this question leads us to a review of the dynamics of bargaining in federal systems.

### **THE FEDERAL BARGAINING GAME**

The bulk of the studies on Russian federalism have viewed center-periphery relations through the lens of an iterative bargaining game, which is a framework often used in the wider comparative literature to examine the dynamics of competition and cooperation among federal and regional politicians.<sup>31</sup> As Ordeshook and Shevstova note, federalism structures an “ $N+1$ ” pattern of political interaction: “ $N$  federal subjects and the

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Economic Role of Political Institutions: Market-Preserving Federalism and Economic Growth,” *Journal of Law, Economics and Organization* 11:1, 1-31.

<sup>31</sup> Steven Solnick, “The Political Economy of Russian Federalism: A Framework for Analysis,” *Problems of Post Communism* (November/December, 1996): 13-19; L. Polishchuk, “The Russian Model of Negotiated Federalism: a Political and Economic Analysis” in Klimanov, V., and Zubarevich, N., eds., *The Regional Dimension of Politics and Economics* (Moscow, St. Petersburg: Studia Politica, 2000). Kathryn Stoner Weiss, *Local Heroes: The Political Economy of Russian Regional Governance* (Princeton, NJ: Princeton University Press, 1997); Daniel Treisman, “The Politics of Intergovernmental Transfers in Russia,” *British Journal of Political Science* 26:3 (1996): 299-336; R. Agranoff, “Federal Evolution in Spain,” *International Political Science Review* 17: 4 (1996): 385-401; William Riker, *The Development of American Federalism* (Boston: Kluwer, 1987). Deil S. Wright, *Understanding Intergovernmental Relations*, 3rd ed. (Belmont, CA: Brooks/Cole, 1988).

national government are adversaries who must compete for power and resources through bargaining, strategic maneuvering, coalition formation and deception.”<sup>32</sup> Except in cases of outright secession, central and regional politicians are bound by a common aversion to the disintegration of the federal state, but they hold divergent interests. Regional governments have an incentive to maximize resources in their respective constituencies, and securing control over them ultimately involves bargaining with the center.<sup>33</sup>

## Strategies

Regional bargaining strategies can range from “assertion” on one end of the spectrum to “loyalty” towards the federal center on the other. Assertive strategies can be viewed as a method of expanding disputes over regionally particular issues to the national political arena via ultimatums, threats, “tax revolts” or other acts of economic and political separatism designed to coerce the center.<sup>34</sup> Various forms of political mobilization, such as holding referenda on a region’s legal status, mass demonstrations, and the creation of political parties with overtly regional agendas, serve the purpose of demonstrating a region’s resolve and enhancing the credibility of future threats. As

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<sup>32</sup> Peter Ordeshook and Olga Shevtsova, “Federalism and Constitutional Design,” *Journal of Democracy* 8: 1 (1997): 27-42.

<sup>33</sup> Generally, the objects of bargaining in federal systems are the rules governing the division of political authority (jurisdictional) and fiscal resources (distributive rules). Intergovernmental fiscal federal rules can be conceptualized in the same manner as a system of property rights: ‘income rights’ – tax sharing norms and the division of natural resource rents; ‘use rights’ – management of state-owned enterprises and regulation of natural resource licensing; and ‘transfer rights’ – control over the privatization of state property. As such, fiscal rules require recognition by both the region and center to provide a degree of certainty and guarantee of autonomy. Autonomy that is simply “grabbed” unilaterally by a region can be usurped just as readily by the federal center. See Charles, McClure Jr., *Fiscal Federalism and the Taxation of Natural Resources* (Toronto: Lexington Books, 1983).

<sup>34</sup> Intergovernmental relations have been framed as an elite bargaining game; instances of assertion are considered to be motivated by regional elites as part of a bargaining strategy to pressure the center into making certain concessions on the federal rules. See, for instance, Hudson Meadwell, “A Rational Choice Approach to Political Regionalism,” *Comparative Politics*, 23: 401-420; Wright, 1988.



opposed to partisan protests, regional assertiveness is characterized by demands for changes in the distribution of political authority (i.e. jurisdictional rules) and fiscal resources (i.e. distributional rules) between the federal center and a particular region or coalition thereof.<sup>35</sup>

As well as an “offensive” variant, where the region is the initiator, regional assertiveness can also take a defensive form, reflected in public defiance of attempts by the central government to encroach upon or rescind autonomy that it had previously granted. Overt resistance to Putin’s campaign to take back much of the formal autonomy devolved under Yeltsin – in particular power-sharing agreements signed with many regions – is a prime example of this. Whatever the form, assertive strategies raise the stakes of the bargaining game for both sides. By contrast, strategies of loyalty are evidenced by political constraint and the avoidance of defiant or provocative actions in the public arena.<sup>36</sup>

Federal strategies range from coercive to accommodative. Coercive strategies indicate that the center is not willing to bargain further than it already has, and usually involve “sticks” to punish regional elites in an effort to deter future acts of offensive regionalism or compel compliance with federal mandates (e.g. counter defensive

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<sup>35</sup> The literature distinguishes between instances of partisanship and regionalism per se. There is a large literature on the effect of partisanship on federal-regional relations. Acts of regional defiance motivated by partisanship are targeted against the policies of the national party in power, and not necessarily motivated by a desire to change the distributional or jurisdictional rules pertaining to a specific region. For an overview of partisanship and federalism, see Alfred Montero, “After Decentralization: Patterns of Intergovernmental Conflict in Argentina, Brazil, Spain and Mexico,” *Publius: The Journal of Federalism* 31:4 (Fall 2001), 43.

<sup>36</sup> It is important to note that the extent of a region’s “loyalty” is relative to the actions of its assertive neighbors and the existing norms of center-periphery interaction (e.g. “rules of the game”), and may not necessarily indicate satisfaction with the existing federal arrangement.

regionalism). Accommodative strategies involve various forms of “carrots,” or concessions, to co-opt regional elites into loyalty. As the central player in the bargaining game, the center’s response to individual instances of regional assertiveness simultaneously structures all regional leaders’ choice sets in terms of the costs of certain types of assertive behavior and rational expectations for accommodation.<sup>37</sup>

### **Federal Outcomes: IGR Typologies**

The interaction of dominant regional and federal strategies corresponds with distinct typologies of intergovernmental relations, or federal outcomes. In reality, federal systems are often hybrids in various policy arenas. The typologies in Table 1.1 are “ideal types,” reflecting the dominant trend characterizing intergovernmental relations in the national political arena at a given phase.<sup>38</sup>

Table 1.1: Federal-Regional Strategic Interaction and IGR Outcomes

Federal Strategy:	Accommodative	Coercive
Regional Strategy:		
“Loyalty” (Restraint)	“Cooperative Federalism”	“Coercive Federalism” (Recentralization)
Assertion	“Assertive Regionalism” (Decentralization)	Intergovernmental Conflict

<sup>37</sup> Ordeshook and Shevtsova, 1997.

<sup>38</sup> The terms describing IGR typologies are borrowed from the comparative intergovernmental literature, though there are many contextual variables in the Russian case that need to be taken into account. For instance, “assertive regionalism” is equivalent to “competitive regionalism” in the literature on developed federations, though the type of competition inferred by competitive regionalism is much more constrained. Competitive regionalism also refers to rivalry among the regions themselves, while the dissertation uses the term assertive regionalism only to refer to the intergovernmental (e.g. federal-regional) dimension of conflict. For an overview of competitive regionalism in the European perspective, See Tanja A. Börzel , “From Competitive Regionalism to Cooperative Federalism: The Europeanization of the Spanish State of the Autonomies,” *Publius: The Journal of Federalism* 30:2 (2000): 127-142.

The first typology, “cooperative federalism”, represents accommodative strategies on the part of both the center and regions. In this case, federalism is “working” according to its intended purpose as a cooperative mechanism for dispute resolution. Competition between the federal and regional governments is restrained as both sides refrain from attempts to unilaterally change the jurisdictional or distributional rules and pursue reciprocity. A key aspect of cooperative federalism is the inclusive nature of decision-making and joint, non-coerced behavior.<sup>39</sup>

Assertive strategies can become dominant if regional elites anticipate that such behavior will lead to some degree of accommodation by the federal center, which may especially be the case if the central government has demonstrated either a lack of political will to punish defiant regions or a credible commitment to enforce uniform rules. Assertive regionalism among wealthier regions is almost always associated with pressures for greater fiscal and political decentralization.<sup>40</sup>

Coercive federalism can be considered the “inverse” of assertive regionalism in that the center takes the offensive, with regional elite generally exhibiting loyalty (acquiescence).<sup>41</sup> The center can use various forms of punishment and compellence, ranging from fiscal pressure tactics and administrative sanctions to criminal

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<sup>39</sup> A key condition of cooperative federalism is that “one plane of government does not coerce the other” and that cooperation is negotiated, which involves some degree of accommodation from both sides. See Joseph Zimmerman, “National-State Relations: Cooperative Federalism in the Twentieth Century,” *Publius: The Journal of Federalism* 31:2 (Spring 2001): 15-35.

<sup>40</sup> See Milica Z. Bookman, *The Political Economy of Discontinuous Development* (New York: Praeger, 1991.)

<sup>41</sup> *Ibid.*, 24. In mature federations, coercive measures by the federal government usually include various forms of federal preemption, as well as fiscal sanctions. While “coercive federalism” has been used to describe regional assertiveness as well in the comparative literature, here it is used solely in regard to the typology of IGR characterized by federal government encroachment and regional acquiescence.

investigations and the threat of brute force. When coercive federalism is the outcome, the costs of resistance (e.g. “defensive” assertion) outweigh the benefits for regional leaders.

In cases where the stakes are high enough that neither side is willing to accommodate the other, intergovernmental conflict may persist, as in the case of the ongoing conflict in Chechnya, which quickly evolved outside the parameters of the federal bargaining game.<sup>42</sup> However, thus far instances of sustained conflict have been the exception rather than the rule, as federal and regional politicians in Russia have shown a propensity for bargaining.

Sustained periods of regional assertiveness can seriously undermine state capacity and engender ethnic conflict, as happened during the Yeltsin years, while coercive strategies by the federal government in direct reaction to regional assertiveness may push Russia closer to the unitary end of the spectrum during Putin's second term. Indeed, for Russia, cooperative federalism – based on norms of accommodation and compromise on both levels of government – could be seen as the most desirable in the interests of deepening democratization.<sup>43</sup>

This brings us to the next logical question: what accounts for the strategic behavior of regional and federal governments? In the Russian case, there has been variation in federal strategies across time – from more accommodative to more coercive, as partisan conflicts that weakened the federal center in the nineties have subsided under

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<sup>42</sup> The proliferation of actors claiming authority on the Chechen side made negotiating difficult if not impossible, while one of the key conditions structuring the federal bargaining game – mutual aversion to state breakdown – was absent on the Chechen side. In the majority of the other internal “ethnic” republics, the Soviet-era leadership remained intact and kept a tight grip on power within the region, adhering to the rules of the game (e.g. limits of permissible behavior) set by Moscow.

<sup>43</sup> See Stepan, 2000 on the importance of the decision-making process for the performance of federal systems in democratizing countries.

Putin. At the same time, there has been considerable continuity in patterns of regional strategic behavior across both the Yeltsin and Putin periods, with some regions consistently pursuing assertive strategies and others remaining loyal. Before examining this variance more closely in the succeeding chapters, however, it is necessary to review the conventional wisdom about determinants of regional strategic behavior in federal systems in general, and in the Russian case in particular.

### **ASSERTIVE REGIONALISM AND RUSSIAN FEDERALISM**

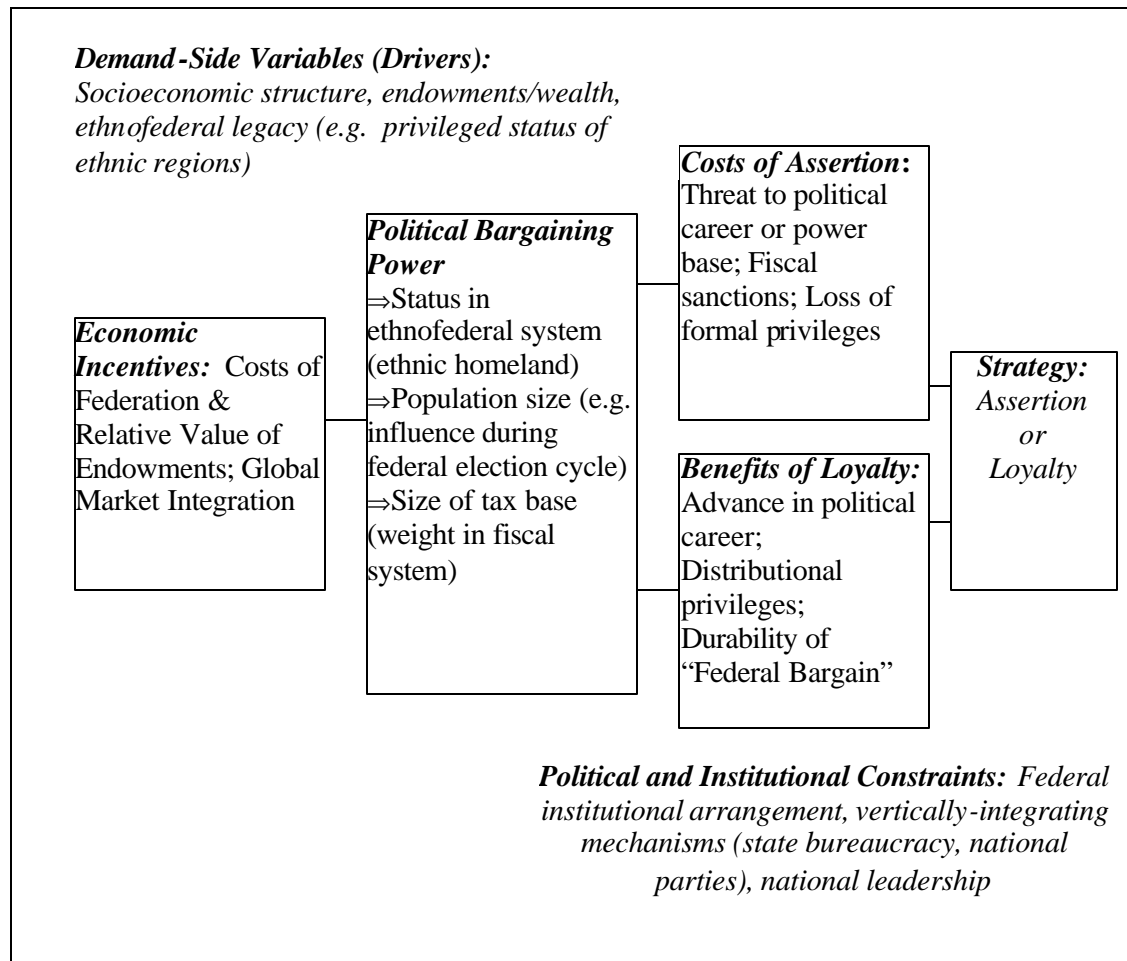
Generally, the literature highlights two main groups of factors as determinants of regional behavior in federal systems. One group of variables, which could be labeled “demand side” factors, gauges the intensity of instrumental incentives for assertion, based on both the potential economic benefits of accommodation by the center as well as a region’s political resources, or bargaining power, in the intergovernmental arena. In the Russian case, these have included regionally-specific factors such as resource endowments, industrial assets and socio-economic structure; the localized impact of global market integration; and status as an ethnic homeland.

Another set of factors includes institutional constraints, which affect the direct costs (e.g. threat of punishment) and opportunity costs (e.g. benefits of an alternative strategy of loyalty) of assertive strategies. Unlike demand-side variables, these factors are not specific to a particular region, but involve some degree of coordination by the central government and are shaped by overall state capacity. Formal institutions include the durability and fairness of the jurisdictional or distributive rules enshrined in the constitution or related legislation, as well as the strength of “vertically-integrating”

mechanisms such as the state bureaucracy and national political party system. Informal institutions include the “rules of the game” of the federal bargaining process – the extent to which federal politicians employ “carrots” or “sticks” that shape regional leaders’ rational expectations of accommodation or punishment. The informal rules governing Russia's federal system have largely been a function of the fluctuating unity of federal elites and the persona and power base of the chief executive, which is particularly linked to the federal election cycle.

Figure 1.1 presents a model of regional strategic decision-making, charting factors that affect the cost-benefit calculations of regional elites, and thus either drive or constrain a strategy of assertion. The individual variables are then examined in more detail below.

Figure 1.1: Summary of Conventional Wisdom about Regional Behavior in Russia<sup>44</sup>



<sup>44</sup> The table reflects an instrumentalist, rather than primordialist view, of ethnic assertion, which is consistent with the conventional wisdom in the Russian-area literature reviewed in this section.

## **“Demand-side” Drivers: Economic Incentives**

Two main categories of economic incentives for assertive regionalism are discussed in the literature: the costs of federation and the relative value of economic assets, including natural resource endowments, industrial wealth and export capacity within a region’s territory.

The costs of federation measure the relative burden placed upon a particular region by the current fiscal federal arrangement, which is primarily a function of its wealth (e.g. tax base).<sup>45</sup> Regions that are net contributors to the federal budget bear the highest costs of sustaining the federation, and thus will benefit most from gaining greater autonomy (fiscal decentralization), rather than transferring their resources to the federal center to subsidize less self-sufficient regions. The level of interregional socioeconomic asymmetry is an important factor that determines the costs of federation placed upon the wealthier regions. As the income gap among regions increases, so does the burden of equalization.

Likewise, the presence of endowments such as natural resources, competitive industries and export commodities motivate attempts to increase a region’s autonomy, especially in the sphere of intergovernmental property rights. The relative fiscal value of these assets is linked to their performance on both national and global markets. In the Russian case, integration with global markets has resulted in a fiscal windfall for exporting regions, whose economies have benefited the most from the change in relative

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<sup>45</sup> Of course political considerations can play a large role in how efficiently the costs of federation are distributed among regions. This is largely a function of a region’s political resources (bargaining power), which is dealt with below.



prices.<sup>46</sup> Indeed, economic globalization has been a major driver of assertive regionalism in mature federal systems as well.<sup>47</sup>

While the relative difference in wealth among regions usually remains constant in the short- to medium-term, asymmetrical economic shocks, such as market reform and major movements on global markets, can increase this gap. Due to the high degree of economic concentration in Russia, market reform initially created a narrow set of “winners” – regions with competitive industrial assets and natural resources – and a much larger field of “losers.” Heightened interregional socioeconomic disparities have forced the center to place higher costs of federation on the winners to reduce the income gap among the two groups and create a more even playing field. Thus, an increasing equalization burden at home and the opportunity to reap the benefits of global market integration provide a constant incentive for the “winners” of Russia’s market transition to strengthen control over rents on their territory via autonomy-seeking strategies.

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<sup>46</sup> The same dynamics affect IGR in mature federations as well. In Canada, for instance, rising oil prices in the seventies prompted oil-producing regions to seek control over a greater share of the windfall. This put them in direct competition with the federal government, which also laid claim to the expanded tax base in order to smooth over the increased income gap between the oil regions and the agricultural, industrial regions. See Charles McLure Jr., *Fiscal Federalism and the Taxation of Natural Resources* (Toronto: Lexington Books, 1983).

<sup>47</sup> See, for instance, Michael Keating, *The New Regionalism in Western Europe: Territorial Restructuring and Political Change* (Cheltenham: Edward Elgar Press, 1998). In addition, Benz notes that in the German case integration with the European Union has caused the more competitive Lander in the West to clamor for greater fiscal and economic autonomy while the more disadvantaged Lander in the East have been seeking greater engagement by the national government (redistribution). See Arthur Benz, “From Unitary to Asymmetric Federalism in Germany: Taking Stock after 50 Years,” *Publius: The Journal of Federalism* 29: 4 (Fall 1999): 55.

## **“Demand-side” Drivers: Political Bargaining Power**

Variations in bargaining power variables can be used to measure the relative political value of a region’s resources and the regional administration’s capacity to use them to pressure the central government. The ability of a region to credibly threaten central objectives such as political stability, re-election of a president or parliament, and smooth tax collection gives it added leverage vis-à-vis the federal center.<sup>48</sup> Regions with higher degrees of bargaining power are predicted to more often “flex their muscles” by pursuing assertive strategies vis-à-vis Moscow.<sup>49</sup>

In Russia, the most potent bargaining chip has been status as an ethnic homeland. Many socialist countries that were divided territorially into titular ethnic homelands have spawned ambitious regional leaders with a political and institutional base for mobilizing resources to assert political and economic autonomy.<sup>50</sup> Russia inherited the Soviet Union’s ethnofederal legacy, whereby regions designated as the historical homelands of titular ethnic groups were distinguished, at least de jure, from the other subjects of the federation. During the collapse of the Soviet Union, the majority of these regions declared sovereignty as internal republics in Russia, and regional leaders’ ability to

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<sup>48</sup> Daniel Treisman, “The Politics of Intergovernmental Transfers in Russia,” *British Journal of Political Science* 26:3 (1996): 299-336.

<sup>49</sup> This is essentially a “Realpolitik” argument: increased capabilities lead to greater assertion.

<sup>50</sup> See Philip Roeder, “Soviet Federalism and Ethnic Resource Mobilization,” *World Politics* 43 (January, 1991), 196-232; Valerie Bunce, *Subversive Institutions: the Design and Destruction of Socialism and the State* (New York: Cambridge University Press, 1999). Bunce asserts that the dense institutional network built by socialist regimes to penetrate society – in essence a de-jure federal institutional structure – played a subversive role during political transitions, leading to state breakdown in the Soviet Union, Czechoslovakia and Yugoslavia.

mobilize ethnic constituencies around regionalist agendas increased the credibility of threats.<sup>51</sup>

Other variables used in bargaining power models include the size of a region's electorate and relative size of a region's tax base. The former reflects a region's potential ability to "blackmail" the center during federal election cycles, and the latter reflects a region's potential ability to threaten federal revenue collection. Relative size matters in terms of bargaining-power: larger regions will, *ceteris paribus*, have more leverage over the center than smaller ones. At the same time, the political value of particular resources in the national arena – and the capacity of the regional regime to mobilize them in a confrontation with the center – will vary across time.

### **Cross-regional studies of assertive regionalism**

Large-n, quantitative studies of regional behavior in the post-Soviet literature have been few. In a study of the entire set of 89 regions through 1995, Dowley finds that instrumental incentives such as net contributor status to the federal budget and the presence of natural resource endowments, as well as the level of bargaining power (ethnic republic status), are positively correlated with regional elite preference intensities for greater decentralization.<sup>52</sup> Likewise, Soderlund finds that structural power resources such as natural resource endowments, industrial wealth, an important geographic location and

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<sup>51</sup> On the various privileges enjoyed by the ethnic republics in Russia's federal system, see Alfred Stepan, "Russian Federalism in Comparative Perspective," *Post-Soviet Affairs* 16: 2 (2000): 133-176.

<sup>52</sup> K. Dowley, "Striking the Federal Bargain in Russia: Comparative Regional Government Strategies," *Communist and Post Communist Studies* 31:4 (1998): 359-380. Dowley performs a content analysis of public speeches, declarations and communications by regional elites.

cultural distinctiveness were bargaining chips that regional elites could use to gain earlier accommodations from Moscow during the bilateral treaty process from 1994-1998.<sup>53</sup>

Treisman's seminal analysis of separatist activism among the subset of Russia's 20 ethnic republics reveals that instrumental incentives such as natural resources, industrial strength and export capacity explain variation in behavior when bargaining power is held constant.<sup>54</sup> Wealthier ethnic homelands (republics) have been much more assertive than poorer ones. Thus, the potential for economic gains is cited as the primary driver of assertive regionalism in the post-Soviet literature on Russia. Bargaining power variables, such as ethnic republic status, explain the timing of a region's actions, and, as will be evidenced below, the strategic response of the center.

### **FEDERALISM UNDER YELTSIN**

In general, demand-side drivers have remained more or less constant throughout the Russian transition.<sup>55</sup> Political-institutional constraints, on the other hand, have varied considerably, due both to changes in the macro-political environment and the strategy of the federal center. This section examines these factors and federal strategy in the Yeltsin and Putin periods in turn.

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<sup>53</sup> Soderlund, Peter J. "The Significance of Structural Power Resources in the Russian Bilateral Treaty Process, 1994-1998," *Communist and Post-Communist Studies* 26 (2003): 311-324.

<sup>54</sup> While there is a debate on whether the centrifugal forces that tore apart the former Soviet Union and Yugoslavia were primarily a function of a primordial drive "from below" for self-determination by various nationalities, or the result of mobilization "from above" by self-interested republican elites, there is a stronger consensus among scholars that separatism and regional defiance in the post-Soviet period have been primarily elite-driven – both among the "ethnic" republics and Russian oblasts alike. Most literature on Russian ethnic separatism gives priority to instrumental motives based on economic calculations. See especially Daniel Treisman, "Russia's 'Ethnic Revival': The Separatist Activism of Regional Leaders in a Post-Communist Order," *World Politics* 49:2 (1997): 212-249.

<sup>55</sup> While the income gap between the richer and poorer regions increased in Russia throughout the nineties, the subset of wealthy regions itself has remained relatively stable.

## Federal Rules

Most scholars concur that there is no particular institutional blueprint for “making federalism work.”<sup>56</sup> At the same time, it is generally recognized that the sine qua non of stable federal systems is an effective and durable “federal bargain” – a viable guarantee against arbitrary interference by the federal government in clearly prescribed spheres of sub-national discretion.<sup>57</sup> To the extent that regional elites have a stake in the federal system, they will eschew assertive strategies that could intensify its instability and result in a new status-quo arrangement that might or might not better serve their particular interests. Concise, fair and well-enforced rules can more effectively co-opt regional elites into the existing federal system and increase the benefits flowing from a strategy of loyalty.<sup>58</sup>

When formal jurisdictional and distributional rules are either ambiguous or not properly enforced by the center, regional elites face a strong incentive to protect themselves from the more immediate threat of federal arbitrariness by pushing for special deals or unilaterally usurping authority and resources (e.g. undertaking “preemptory” assertive strategies in face of uncertainty). For example, in the Yeltsin period the dearth

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<sup>56</sup> See, for instance, Ronald Watts, *Comparing Federal Systems* (Montreal and Kingston: McGill-Queen’s University Press, 1999). Comprehensive cross-comparison of federations – in terms of the division of jurisdictional powers, distribution of fiscal resources and the corresponding level of centralization or decentralization – is an extremely complex task in itself.

<sup>57</sup> Riker, 1964.

<sup>58</sup> According to Riker, political elites who negotiate a federal bargain do so out of a belief that their interests are better served by the federal arrangement rather than a unitary or confederal one. Thus autonomy-seeking regional elites may prefer to make concessions at some point if the federal rules are stable and fair, rather than taking the risk of pursuing assertive strategies that could eventually spark an economic crisis or political instability, leading to either to a clamp-down by the federal government (move toward unitary system) or state breakdown (confederal system).

of federal legislation clarifying the divisions of power among levels of government, together with the weakness of the Constitutional Court, set the stage for an ad-hoc process of state-building whereby regional elites repeatedly attempted to “grab” power from below in the context of a virtual legal vacuum.<sup>59</sup>

The legitimacy of the federal decision-making process itself is also an important variable affecting the strength of a federal bargain. The division of powers at federal and regional levels, including a bicameral legislature, is designed to create consensus among the regions and balance the federal decision-making process. In the Russian case, the large powers afforded to the president by the Russian Constitution, coupled with the even stronger position of most regional executives vis-à-vis legislative bodies, heavily favors executive bargaining and bilateral deals.<sup>60</sup> The lack of transparency in the process of negotiating power-sharing agreements between federal and regional executives led to widespread perceptions of unfairness by regions that felt they had been slighted, while enforcement of the agreements was problematic as many of them contradicted the federal Constitution.<sup>61</sup> In addition, special fiscal deals with the central government that allowed certain wealthy regions (mainly the “ethnic republics”) to free-ride further raised the costs of federation for the remaining net contributor regions, in turn fueling assertion.<sup>62</sup>

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<sup>59</sup> Kathryn Stoner-Weiss, “Central Weakness and Provincial Autonomy: Observations on the Devolution Process in Russia,” *Post-Soviet Affairs* 15:1 (1999): 87-106.

<sup>60</sup> Ordeshook and Shevtsova, 1997.

<sup>61</sup> Stoner-Weiss, 1999.

<sup>62</sup> Even if distributional rules are asymmetrical (e.g., favoring one region over others), the decision-making process is paramount to ensuring consensus. Federal legislative venues such as parliament are the only ones which collectively include representatives from all regions in the decision-making process. For example, Stepan, notes that the decision to grant Spain’s autonomous regions special status was made collectively at the national level (parliament) rather than as a special deal between executives. The result

Thus, the role of the federal institutional arrangement during the 1990s – in particular the dearth of clear and durable rules and a lack of transparency in the federal decision-making process – encouraged regional assertion. Regional elites had small stakes in the federal system, and fewer incentives to adopt a strategy of loyalty. Federal legislation, rather than executive orders and bilateral agreements, would have provided greater legitimacy to the federal decision-making process and produced a more durable “federal bargain” for regional elites. Yet, Yeltsin’s narrow base of support in the Duma, coupled with the regional governors’ ex-officio status as senators in the upper chamber, made coordination between the executive and legislative branches extremely problematic.<sup>63</sup>

### **Vertically Integrating Mechanisms**

Irrespective of federal constitutional design, political coordination between levels of government depends on the effectiveness of vertical-integrating mechanisms that project the central government’s influence into the periphery. These mechanisms include the state executive hierarchy (e.g. formal links between federal and regional bureaucracies), which enforces compliance with rules and oversees the implementation of federal policies, as well as political parties, which serve to align the interests of regional and national politicians.

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was greater intergovernmental stability and consensus during the transition, as opposed to the Russian case. Stepan, 2000.

<sup>63</sup> Indeed, many observers point to the volatility in executive-legislative relations on the federal level as Yeltsin’s Achilles heel in center-periphery relations. See Stoner-Weiss, 1999 and 2001.

*State Executive Hierarchy:* Mechanisms by which the executive branch can monitor regional elites and enforce the rules are an integral element of political coordination in decentralized systems. When the state executive hierarchy is strong and responsive, the federal center will have access to both fiscal and political resources in a region that can be used to increase the center's leverage over regional officials.<sup>64</sup>

Under Yeltsin the administrative capacity of the central state to check regional behavior, coordinate federal functions and implement policy in the periphery was severely limited. The key links between the Kremlin and regional administrations, the presidential representatives, were rendered ineffective because they depended on regional budgets for housing and other expenditures, were understaffed, and in many cases had pre-established close ties with regional elite groupings, all of which made them prone to "capture" by sub-federal governments.<sup>65</sup> Furthermore, various regions gained control over appointments to branches of the Federal Prosecutor's office and security agencies as part of their deals with the federal center.<sup>66</sup>

*Political Parties:* The state administrative hierarchy is primarily a "top-down," or coercive mechanism. Regional elites are inclined to either capture agencies and their

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<sup>64</sup> For instance, in the Chinese case, Li and Lian identify "checking" and "enforcement" agencies as crucial to the center's capacity to gather information and discipline officials in the periphery. Checking mechanisms include the prosecutor's office as well as various intergovernmental commissions to root out corruption, while "enforcement" mechanisms, such as arbitration courts, monitor adherence to legal norms in doing business (bankruptcy, contracts, etc.). The authors argue that decentralization and autonomy are necessary, but not sufficient, elements for ensuring effective market reform in China: autonomy must be balanced by control. See Shuhe Li and Peng Lian, "Decentralization and Coordination: China's Credible Commitment to Preserve the Market under Authoritarianism," *China Economic Review* 10 (1999): 161-190.

<sup>65</sup> Interview with Vladimir Reshetnikov, government official in Kirov Oblast, June 2000. The presidential representative and his staff were regularly unable to perform many of their assigned functions, and members of the governor's staff had to fill the void.

<sup>66</sup> Stoner-Weiss, 1999.



representatives or otherwise curtail their influence.<sup>67</sup> National political parties, on the other hand, also have the capacity to co-opt regional elites by linking their political ambitions with those of national politicians (re-election) and enhancing the representation of regional interests at the national level.<sup>68</sup> In terms of the intergovernmental bargaining game, national parties can structure cooperative, or “win-win,” outcomes in federal systems.<sup>69</sup>

When regional political actors are not bound by loyalty to a national party for the advancement of their political career, the central government must employ other bargaining methods (e.g. fiscal carrots or political sticks), which can eventually exhaust central resources.<sup>70</sup> Political parties can also supplement the functions of state bureaucratic mechanisms by themselves as coercive instruments. For instance, one of the key factors behind China’s success in coordinating political decentralization is the role of the Chinese Communist Party; the central government uses regional leaders’ desire for advancement in the party to compel them to obey central objectives.<sup>71</sup>

Thus, when national party systems are strong, the costs of defiance of the center will be higher, to the extent that the party leadership is able to discipline recalcitrant regional

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<sup>67</sup> Li and Lan, 1999.

<sup>68</sup> On the importance of party systems, see Herman Bakvis and William Chandler, *Federalism and the Role of the State* (Toronto: University of Toronto Press, 1987).

<sup>69</sup> Indeed Ordeshook and Shevtsova note that “No [intergovernmental] agreement is likely to withstand demands for renegotiation... sustaining a federal arrangement that leaves federal subjects in possession of certain exclusive and very important portions of sovereign power requires institutional arrangements that make it in the self-interest of regional political elites to cooperate and coordinate with one another and with the national government, and makes it in the self-interest of national elites, including those not specifically thought to represent regional governments, to be protective of the autonomy of all federal subjects.” They make the case that a strong national party system can fulfill this role. (32) See Ordeshook and Shevtsova, 1997.

<sup>70</sup> Kathryn Stoner-Weiss, “The Limited Reach of Russia’s Party System: Underinstitutionalization in Dual Transitions,” *Politics and Society* 29:3 (September 2001): 385-414.

<sup>71</sup> Blanchard and Schleifer, 2000.

politicians by threatening their careers and power bases. Conversely, the benefits of loyalty will be higher, because federal politicians have a mechanism with which to advance or retard regional politicians' careers.

The weakness of the Russian national party system in the 1990s significantly diluted its vertically integrating function – e.g., its capacity to act as a systematic tool of either co-optation or coercion – in intergovernmental relations. Partisan identifications among executives in Russia, especially at the regional level, were weak due to the nature of the electoral rules, the sequencing of federal and regional elections, the lack of strategic voting in the population, and the reluctance of the chief executive to associate himself directly with a party.<sup>72</sup>

### **Rules of the Game under Yeltsin**

Finally, the informal rules of the bargaining game -- the center's reputation and strategy in the intergovernmental political arena – shape regional behavior in federal systems.<sup>73</sup> Consistent federal strategies shape rational expectations of what the immediate response to assertiveness will be. While there are many factors that determine the response of a federal government to regional assertiveness, the relative unity/disunity of federal elites and the leadership style of the chief executive play a particularly important role in the Russian case.

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<sup>72</sup> On the underinstitutionalization of Russia's party system, see especially Robert Moser, "Electoral Systems and the Number of Parties in Post-Communist States," *World Politics* 51 (April 1999): 359-384; and Stoner-Weiss, "The Limited Reach of Russia's Party System: Underinstitutionalization in Dual Transitions," 2001.

<sup>73</sup> Steven Solnick, "The Political Economy of Russian Federalism: A Framework for Analysis," *Problems of Post Communism* (November/December, 1996): 13-19.

As Higley and Burton have noted, the balance of power among elite groups competing for power influences the nature of the rules of the game, and the probability that formal rules will be adhered to by all sides.<sup>74</sup> The configuration of federal elites reflects the central government's ability to act as a unified front and maintain a credible threat (e.g. commitment to coercive strategies) in order to deter or coerce regional elites. When federal elites are divided, and locked in an unrestrained or "winner-take all" conflict, vying factions are more likely to use selective concessions to enlist the support of regional elite groups to boost their position in the struggle with rival groups in the central political arena. Repeated strategies of accommodation by opposed factions deprive the federal center of a reputation for enforcing fair, symmetrical rules, which in turn fuels further instances of assertive behavior from below.

During most of the Yeltsin period, a high level of partisan (ideological) polarization among federal political elites, coupled with internecine privatization struggles among various informal political "clans", undermined the center's cohesiveness as a united front and sapped its political will to coerce regional elites systematically. In particular, the high level of political uncertainty at the federal level stemming from the threat of a Communist revanche put the Kremlin in a very weak bargaining position— and an overly generous mood -- during federal election cycles.<sup>75</sup> Moreover, Yeltsin's personal leadership style, which was based on informal ties, face-to-face haggling, and

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<sup>74</sup> Typologies of elite configurations can be found in John Higley and Michael Burton, "Elite Transformations in Democratization's Three Waves," Paper presented to IPSA World Congress, Quebec, 2000. When elites are disunited, there is a lack of consensus on the rules of the game, and competition takes place in the context of a "winner take all" environment. A "consensually united" elite adheres to set rules and codes of political competition.

<sup>75</sup> Solnick, 1996.

backroom deals, further undermined the center's credibility and perceptions of its fairness.<sup>76</sup>

Both formal and informal constraints on regional behavior were severely limited, in short. A recalcitrant parliament, a state administrative hierarchy "captured" from below, disunity among federal elites – in addition to Yeltsin's own lack of popular support – all deprived the central government of the capability and political will to systematically pursue coercive strategies in the formal arena and raise the costs of regional assertion. At the same time, the weakness of the "federal guarantee," lack of transparency in the executive bargaining process, and under-institutionalization of the national party system prevented the cooptation regional elites. Federal leadership encouraged, rather than discouraged, assertive regional strategies.

In response to the rising tide of assertive regionalism, the Kremlin adopted a dominant strategy of selective accommodation, although there were isolated cases of successful coercive strategies (e.g. punishment).<sup>77</sup> The Kremlin strategically appeased assertiveness and rewarded loyalty by manipulating distributive and jurisdictional rules. For instance, according to Treisman, the Kremlin used budgetary transfers to appease regions that demonstrated the most credible threats to the regime.<sup>78</sup> Likewise, Solnick

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<sup>76</sup> On the importance of such informal relationships see James Hughes, "Moscow's Bilateral Treaties Add to the Confusion," *Transition* 2, 19 (1996):39-43.

<sup>77</sup> For instance, after the first wave of regional assertiveness in 1993, several governors were dismissed by Yeltsin. The Kremlin's ability to punish regional executives was greatly reduced after gubernatorial elections were introduced around the country in 1995-6, as evidenced by Yeltsin's unsuccessful campaign to unseat Primorie governor Yevgeny Nazdratenko in the latter part of the nineties. Nazdratenko, one of the more assertive (and corrupt) regional executives, was finally persuaded by Putin to leave office after receiving a position on a federal commission.

<sup>78</sup> Daniel Treisman, *After the Deluge: Regional Crises and Political Consolidation in Russia* (Ann Arbor: University of Michigan Press, 1999).

notes that the Kremlin manipulated other selective incentives – such as the signing of power-sharing treaties – in order to co-opt regions and break up regional coalitions.<sup>79</sup> Additionally, the Kremlin rewarded loyal regions that supported the “party of power” in federal elections.<sup>80</sup> But the resulting system of federal rules was highly asymmetrical and ad-hoc, and the ethnic republics as a group were able to gain more jurisdictional and distributional privileges than the non-ethnic regions.<sup>81</sup>

While the center’s strategy of selective accommodation was ultimately successful in staving off the threat of territorial disintegration and preserving the regime, the Kremlin’s “generosity” in the intergovernmental arena eroded its ability to coerce regional elites while at the same time exhausting its capacity for further accommodation. In turn, weak political coordination of economic decentralization resulted in a crisis-prone fiscal federal system and a fragmented national market.<sup>82</sup>

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<sup>79</sup> Solnick, 1996.

<sup>80</sup> Vladimir Popov, “Fiscal Federalism in Russia: Rules Versus Electoral Politics,” Working Paper, <http://www.nes.ru/public-presnetations/Papers/Popov.htm>, accessed on December 13, 2002.

<sup>81</sup> M. Guboglo, *Federal Power and the Power of Federalism* (Moscow: State Duma, Committee on Federal and Regional Policy and the Russian Academy of Sciences, 1997). Differences in formal accommodation within each set of regions were mainly reflected in the timing of treaty-signing, in addition to the specific needs of individual regions.

<sup>82</sup> Russia’s fiscal federal system in the nineties has been described as “market-distorting,” in that the state’s inability to enforce a common market and legal space, discipline regional leaders and efficiently distribute resources resulted in poor economic performance. See Darrell Slider, “Russia’s Market-Distorting Federalism,” *Post-Soviet Geography and Economics* 38 (October, 1997): 445-460. On the dangers of economic decentralization without adequate central political coordination, see also Wibbles, 2000.

## FEDERALISM UNDER PUTIN

Putin's ascendancy to power ushered in a new phase of intergovernmental relations marked by a turn toward political and fiscal centralization.<sup>83</sup> Putin's initial political assets included his popular appeal stemming from his image as a strong statesman, as well as his amenability to both the Communist opposition and competing federal political-financial clans.<sup>84</sup> Indeed, the federal elite's loose rallying around the political persona of Putin has helped pave the way for some degree of change in virtually all of the supply-side factors during his first term in office.

### Formal Rules and Federal Institutions

First and foremost, the Kremlin's ability to broker a settlement with the Communist opposition in parliament and form a centrist majority ended the hostile executive-legislative relations that plagued his predecessor. This in turn allowed the Kremlin to spearhead legislation overhauling Russia's federal institutional arrangement. The main thrust of Putin's reform project has been reducing the political influence of regional executives over the national legislative process and over federal bureaucracies in the periphery, while also establishing clear, symmetrical federal rules. By moving the main venue of decision making on intergovernmental issues from the executive (e.g. bilateral deals) to parliament, Putin has sought to increase the transparency and legitimacy of federal rules.

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<sup>83</sup> As Dogan and Higley argue, periods of crisis have a profound effect on the configuration of national elites, and consequently, the future political trajectory of transitions. Mattei Dogan and John Higley, *Elites, Crises, and the Origins of Regimes* (Lanham, MD: Rowman & Littlefield Publishers, 1998).

<sup>84</sup> Peter Reddaway, "Will Putin be able to Consolidate Power?" *Post-Soviet Affairs* 17:1 (2001): 23-44.

One of his first moves was to rescind the governors' ex-officio status in the upper house of parliament, replacing them with representatives that resemble senators in other federations. While they are still appointed by regional governments, the fact that they are once-removed from the governors has increased the loyalty (pliability) of the upper house vis-à-vis Kremlin. Furthermore, Putin has instituted formal procedures for the removal of governors from office by federal courts in cases of criminal activities or administrative incompetence.

In the fiscal federal arena, Putin has overhauled the tax system, resulting in the further recentralization of fiscal resources, a trend that began following the 1998 fiscal crisis. In addition, the federal government has curtailed many of the distributional privileges afforded to individual regions, including the ethnic republics, by his predecessor. In order to clarify jurisdictional rules, Putin established a presidential commission to formulate legislation demarcating intergovernmental competencies. One of the key priorities in this sphere is strengthening the fiscal sufficiency of municipal governments.<sup>85</sup>

Concomitant with the legislative process, the Kremlin has pressured regional leaders to voluntarily abrogate the power-sharing treaties signed with the central government in the mid- to late nineties, which are the principal legacy of the Yeltsin period. In general, the redesign of the federal institutional arrangement – from a high degree of asymmetry and opaqueness to more concise, durable and fair rules – is aimed at

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<sup>85</sup> In late 2002, Dimitry Kozak, head of the Commission, stated that he would recommend over 200 separate pieces of legislation that would demarcate federal and regional competencies. More self-sufficient municipal government would also serve a political purpose by empowering mayors, who have traditionally been highly dependent on regional administrations for funding, to counterbalance the near-authoritarian power of some regional executives within their jurisdictions.

reducing the grounds for contention and increasing the stake that a greater number of regions have in the “federal bargain.”

### **Vertically-Integrating Mechanisms**

*State Administrative Hierarchy:* Putin has made restoration of the “vertical” dimension of state authority, or the executive hierarchy, a top priority. His major innovation in this regard has been dividing the country into seven macro-regions (federal districts) and appointing commissars attached to the presidential administration to oversee the implementation of federal directives. Most of the new commissars have a background in the security forces or military.<sup>86</sup> The main task assigned to the federal districts has been to bring regional legislation into line with the Russian Constitution, and stimulate outside investment in the regions. In addition, Putin has used other state agencies, such as the Prosecutor General’s Office and Federal Security Agency, to influence the political situation in assertive regions.<sup>87</sup>

*Political Parties:* Although Putin has not formally joined a national political party, his popularity has the potential to boost the status of the “party of power,” which enjoyed very limited support under Yeltsin. The largest pro-Kremlin party, United Russia, has had more success than previous parties of power in garnering nationwide support, and, has developed into a popular centrist party.<sup>88</sup> A more popular “party of power” would in turn

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<sup>86</sup> Reddaway, 2001.

<sup>87</sup> Under Putin, both the Prosecutor General’s office and the Federal Security Agency have been used in attempts to influence the outcomes of regional elections, at times successfully, as evidenced by the unseating of Yeltsin-era incumbents in the republics of Yakutia and Ingushetia.

<sup>88</sup> Reddaway, 2001. In the 1999 parliamentary elections, Unity gathered almost three times as much votes as the previous party of power (Our Home is Russia) in 1995.



raise the benefits of loyalty for governors, increasing the center's ability to co-opt regional elites.<sup>89</sup>

### **Rules of the Game under Putin**

The center of the political spectrum – virtually non-existent at the beginning of the transition– has widened significantly as Russia's political space has become less ideologically polarized. As a result of a convergence toward the political center, patterns of elite interaction in the federal political arena have become more cooperative and the threat of a Communist *revanche* has faded.<sup>90</sup> As the federal center has started to coalesce into a united front (at least in public), the pivotal role of the regions as powerbrokers in the federal arena has been reduced and, correspondingly, the political will of the federal center to rein in regional leaders has increased. Furthermore, Putin's own background in the KGB and his personal connections with the nation's "security elite" (*e.g. siloviki*) have given him more authority among regional leaders than his predecessor had.<sup>91</sup>

On one hand, the Kremlin under Putin has been successful in deterring offensive forms of assertive regionalism, due to its increased credibility and the strengthened political will of a united federal center. On the other hand, the Kremlin has enjoyed only limited success in battling defensive forms of assertive regionalism. Several regions have overtly resisted Putin's directive that regional leaders abrogate their power-sharing agreements,

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<sup>89</sup> Recent legislation requires that a certain portion of regional deputies must be elected on national party tickets.

<sup>90</sup> In addition to brokering a tactical alliance with the opposition in parliament, Putin has done a better job of regulating the inter-elite struggles for property that seriously divided the Yeltsin administration; some of the Yeltsin-era "oligarchs" (*e.g.* V. Gusinsky and B. Berezovsky) were driven from the country.

<sup>91</sup> Reddaway, 2001.

with some still holding out to this day.<sup>92</sup> In addition, the newly instituted federal district apparatus has also made limited progress in forcing regions to conform to federal policy.<sup>93</sup> Putin has thus far acted with caution toward defiant regional elites, and has yet to employ the legislation that permits the removal of governors from office. On the contrary, many assertive regional leaders have secured the formal right to run for re-election for third and fourth terms. Indeed, Putin's avoidance of confrontation and his apparent willingness to pursue accommodative strategies has prompted some observers to claim that he is reverting to "Yeltsinism," and that his formal authority has not translated into the actual capacity to coerce regional elites.<sup>94</sup>

## CONCLUSION

Given the weakness of political and institutional constraints on regional behavior, the wave of "offensive" assertive regionalism that characterized the first decade of Russia's federal transition was not surprising. Neither is the fact that under Putin a more united federal center and strengthened executive hierarchy has placed assertive regions on the defensive. This sharp swing of the federal pendulum approximates a "revolution from above", and is consistent with Russia's historical pattern of recentralization after periods of weakness and crisis.

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<sup>92</sup> The Kremlin has not unilaterally voided the power-sharing agreements; instead, regional leaders and the Kremlin have signed a bilateral document nullifying the previous treaty. The presidential envoys in particular have been given the task of pressuring regional leaders to "voluntarily" give up the agreements.

<sup>93</sup> Peter Reddaway, "Is Putin's Power More Formal than Real?" *Post-Soviet Affairs* 18:1 (2002): 31-40.

<sup>94</sup> Daniel Treisman, "How Different is Putin's Russia?" *Foreign Affairs* 81:6 (2002). Treisman asserts that Russia's federal system is still akin to the Yeltsin-era model of "Feuderalism." Specifically, Putin has relied on special deals with regional elites rather than asserting his formal authority in intergovernmental relations, while the presidential envoys have been hampered by overlapping jurisdictional boundaries and unclear mandates.

At the same time, scholars point increasingly to patterns of continuity between the two presidencies. Despite the expanded arsenal of political and formal state resources at his command, Putin has had mixed success in compelling regions to break their practices during Yeltsin period. The next chapter examines a relatively uniform pattern of assertive regionalism under both Yeltsin and Putin that is not adequately explained by either the demand-side factors or institutional approaches to regional strategic behavior that are outlined in the literature. It is argued that there is an additional variable structuring center-periphery relations and accounting for sub-national variation.

## **Chapter 2: Big Business in the Intergovernmental Arena**

An examination of regional strategic behavior across both the Yeltsin and Putin periods reveals a dichotomous pattern that defies conventional wisdom. Russia's wealthiest regions can be divided into two groups – “assertive” and “loyal” – despite the fact that they have equally high levels of instrumental motives for pursuing assertive, autonomy-seeking strategies. While the ethnofederal system inherited from the Soviet Union explains part of this dichotomy, it cannot account for the divergence of behavior within subsets of ethnic and non-ethnic regions, which are found in both the “assertive” and “loyal” categories. Moreover, the dichotomous pattern has remained consistent across time despite the redesign of federal institutions, strengthening of the executive apparatus, and changes in national leadership.

In this chapter, I develop a theoretical perspective for explaining the divergence in levels of assertive behavior among Russia's wealthier regions. I make the case for incorporating a missing variable – the role of national-level businesses – into customary explanations of assertive regionalism. I argue that the top echelon of large businesses in Russia has a greater propensity to ally with the federal center, enhancing its capacity to both coerce and co-opt elites in the wealthier regions. I then develop a theoretical framework for viewing national-level businesses as both “sticks” and “carrots” on the regional level that can reduce the economic incentives and political opportunities for

assertive behavior. In the chapter's concluding section, implications for both Russian area studies and the wider comparative field are examined.

### **THE PUZZLE OF RUSSIAN FEDERALISM**

The “winners” of Russia’s market and federal transition – wealthier regions that enjoy natural resource endowments and competitive industrial bases – have exhibited a wide degree of variance in strategic behavior in the intergovernmental arena. Russia’s wealthy regions can be divided into two distinct subsets. The first subset has consistently pursued assertive strategies, including provocative acts of political and economic separatism under Yeltsin, as well as overt resistance to Putin’s attempts to rescind the formal autonomy previously devolved through bilateral power-sharing agreements. The second subset, however, has more often followed strategies of loyalty, exhibiting greater restraint in the public political arena under Yeltsin, and more readily acquiescing to Putin’s mandates.

Table 2.1: Strategic Behavior of the Wealthy Regions<sup>95</sup>

<i>Dominant Strategy</i>	<i>Assertion</i>	<i>“Loyalty”</i>
<b>“Offensive” Regionalism (Yeltsin period)</b>	Demands for changes in legal status, political ultimatums, “tax revolts”, etc.	Restraint; less unilateralism and confrontational behavior in the public arena
<b>“Defensive” Regionalism (Putin period)</b>	Overt defiance of Kremlin’s mandate to abrogate power-sharing treaties	Quicker compliance with, and public support for, abrogation of power-sharing agreements
<b>Type of Political Mobilization (Both Periods)</b>	<i>Regionalist</i> : Active participation by executive in regionalist parties; referenda on autonomy; early elections	<i>National</i> : Greater support by executive for pro-Kremlin “parties of power;” low levels of regionalist party building

Likewise, regional executives in the “assertive” group have consistently pursued strategies of mobilizing regionalist parties and referenda, while the “loyal” executives have generally eschewed regionalist mobilization and more actively supported national, pro-government parties during federal election cycles.<sup>96</sup>

At first glance, a simple explanation for the consistency in regional strategies across both periods is that regions which were the most assertive under Yeltsin – and therefore gained the most in terms of special privileges – now have the most to lose under Putin. However, the problem is more complex. With few exceptions all the wealthy

<sup>95</sup> The upper half of Russian regions, ranked by per-capita industrial output, is the main focus of this study (wealthiest 44 of the 89 total regions). A detailed breakdown of the regional assertiveness index, including types of actions and weightings, is presented in chapter 4.

<sup>96</sup> It is important to note that the extent of a region’s “loyalty” is relative to the actions of its assertive neighbors and the existing norms of center-periphery interaction (e.g. “rules of the game”), and may not necessarily indicate satisfaction with the existing federal arrangement. For regional executives, remaining “quiet,” and supporting the national party of power during federal election cycles may be considered a strategy of loyalty when other regional leaders are pursuing assertive strategies and building regionalist parties. In times where the center takes the offensive, loyalty is reflected in acquiescence to central mandates. The ends pursued via a strategy of loyalty can be the same as those pursued by strategies of assertiveness – accommodation by the center – but the means, and therefore the qualitative nature of intergovernmental relations, are profoundly different in this case. A strategy of loyalty is based on expectations of reciprocity, in that the region expects to be rewarded at a later point, while assertive strategies are based on unilateral actions and threats to coerce the center into accepting the region’s terms and timing. Chapter 5 addresses the importance of timing of regional assertiveness.

regions signed bilateral agreements in the 1990s, formally delineating their autonomy with the center and expanding their control over resources in their territories. The “quieter” regions that were rewarded for their loyalty under Yeltsin could be expected to resist the central government’s recent campaign to revoke their autonomy alongside the more assertive ones that pioneered the drive.<sup>97</sup>

In fact, this did occur for a certain period of time. Almost all of the wealthy regions – from both the “assertive” and “loyal” camps – banded together to resist the mounting trend toward political and fiscal recentralization that occurred in the wake of the August 1998 financial crisis.<sup>98</sup> Soon after Putin’s electoral victory, however, the Kremlin launched a campaign to curtail the regions’ political and fiscal autonomy, and the wealthy regions eventually split back into “defiant” and “loyal” camps, suggesting that the central government wields an additional source of political leverage over the loyal regions.

“Demand-side” factors, which gauge the level of instrumental motives for assertive strategies, are unable to explain the divergence in behavior among the wealthy

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<sup>97</sup> A high level of assertiveness was neither a necessary nor sufficient condition for receiving special accommodation from the center in the form of a bilateral agreement (See table 4.7 below). The difference in formal accommodation of the wealthy regions was primarily in the timing of actions, such as the signing of bilateral agreements delineating intergovernmental competencies, and the authorization of regional elections. In general, the assertive group pioneered both processes, signing power-sharing agreements and holding regional elections earlier than the loyal group. While some of the features of the power-sharing agreements were symbolic and not consistently implemented by the federal center, they held significant political value for the governors, both in terms of gaining access to more fiscal resources on their territory and increasing their authority in the region as “political heavyweights” able to effectively bargain with the center.

<sup>98</sup> This was especially evident during the federal election cycle in 1999-2000, when most of the wealthy regions banded together under the banner of the “Fatherland-All Russia” party, which had a clear agenda to defend regional autonomy, in particular the power-sharing agreements. The party’s presidential hopeful, Evgeniy Primakov, had renewed the federal government’s bilateral agreement with Tatarstan during his tenure as Prime Minister.

regions. All the wealthy regions have high levels of economic incentives for pursuing strategies of assertive regionalism, in both its offensive and defensive forms, according to traditional measures such as aggregate levels of natural resources, export capacity and industrial output. Likewise, regions in both camps have been net donors to the federal budget for extended periods throughout the transition. Interestingly, observations are often counterintuitive in this regard: many of the regions in the “loyal” camp have been net contributors to the budget for the longest periods of time, and they enjoy the highest levels of per-capita exports and industrial output.<sup>99</sup>

Asymmetrical levels of political bargaining power do explain part of the variation. Russia’s internal “ethnic” republics have enjoyed greater political leverage vis-à-vis the Kremlin due to their privileged political-institutional status as official homelands of non-Russian ethnic groups, which is a legacy of the Soviet ethnofederal system. Indeed, the wealthiest ethnic republics have been the most assertive throughout the transition period, which is consistent with the literature on ethnicity-based resource mobilization in the post-Soviet period.<sup>100</sup>

However, ethnic homeland status can only explain the divergence in behavior between, but not *within*, the various tiers of regions. For instance, the “Russian” regions that do not have ethnic homeland designation (*oblasts and krays*), which make up the majority of the wealthy cohort, are almost equally divided between loyal and assertive.

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<sup>99</sup> The list of regions classified as net contributors, or “donors” to the federal budget changes from year to year. Some regions have been consistently on the list, and are classified by the Ministry of Finance as having the highest category of fiscal sufficiency.

<sup>100</sup> A dummy variable identifying ethnic homelands is significant when regressed against the index of assertiveness. This is consistent with the literature. See Daniel Treisman, “Russia’s ‘Ethnic Revival’: The Separatist Activism of Regional Leaders in a Post-Communist Order,” *World Politics* 49:2 (1997): 212-249.



Here, other bargaining power variables found in the literature, such as population size, tax base, etc. do not adequately explain the difference.<sup>101</sup>

The puzzle becomes even more acute when we turn our attention from “demand-side” factors to the central state’s capacity to consistently enforce political and institutional constraints on assertive behavior.<sup>102</sup> The relative difference in regional behavior has persisted under both Yeltsin and Putin, despite significant variation in federal institutional arrangements, the strength of vertically-integrating mechanisms including the executive hierarchy and the “party of power”, and national leadership (e.g. elite unity and executive leadership styles). Thus, personal ties or fiscal appeasement might explain repeated strategies of loyalty under Yeltsin, but they do not explain why these same regions would also be more acquiescent under Putin. It is certainly true that Putin has been much more successful than his predecessor in deterring politically disruptive acts of regionalism. Yet, Putin has had mixed success in compelling various regions to dismantle the Yeltsin legacy, and he has been occasionally forced to negotiate with recalcitrant regional executives.<sup>103</sup>

This pattern suggests that there is a missing variable not accounted for by the literature that explains the center’s greater success in coercing or co-opting one subset of the wealthier regions but not the other. Identifying this variable is important to understanding factors that affect the political integration of democratizing federal states.

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<sup>101</sup> See Figure 1.1 in Chapter 1 for an overview of economic incentives and bargaining power variables.

<sup>102</sup> These include the durability and legitimacy of the current federal institutional arrangement; the strength of “vertically-integrating” mechanisms such as the state bureaucracy and political party system; and national leadership – the unity of federal elites and the persona of the chief executive – which shapes regional leaders’ rational expectations about the center’s immediate response to a given strategy.

<sup>103</sup> This has been particularly true closer to federal election cycles; see Chapter 3 for a more detailed discussion.

## SOLVING THE PUZZLE

Approaches that use aggregate measures of economic or political resources to gauge the level of instrumental incentives for regional assertion make certain implicit assumptions about collective action by regional elites. For instance, approaches that highlight economic incentives assume that regional politicians aim to increase their authority by obtaining greater control over rents in their jurisdictions and then distributing these to key constituencies.<sup>104</sup> Likewise, bargaining power approaches assume that regional administrations have the capability (or can credibly threaten) to mobilize resources in confrontations with the center.

Accordingly, both of these approaches assume demand for – or at least tacit support of – an assertive, autonomy-seeking strategy by major constituencies that seek special privileges, such as enterprise directors or leaders of titular ethnic nationalist groups. However, when influential actors within a region oppose a confrontation with the federal center, the political utility of assertiveness for regional politicians decreases, while divisions in the regional elite reduce the regional administration's ability to act as a united front. This in turn diminishes regional bargaining power vis-à-vis the center. Due to the high degree of industrial concentration in Russia, big business actors control a significant amount of economic resources and wield a high degree of political influence at the regional level, especially in the wealthier regions.

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<sup>104</sup> Of course personal financial gain (e.g. corruption) may have played a role as well, but the dissertation assumes that a strategy of assertion is supported by a wider group of elites that wish to receive greater fiscal privileges or political authority from Moscow.

According to the dominant perspective in the literature, big business is part of the problem of assertive regionalism. Customarily, business actors are assumed to be in collusion with regional governments in pursuing assertive, rent-seeking strategies.<sup>105</sup> Indeed, the instrumentalist view of ethnicity-based regional assertion assumes that regional leaders play the “ethnic card” to expand their influence over the region’s key economic assets, either directly by winning greater control over the privatization process, or indirectly by redistributing a larger portion of federal income to regional constituents.<sup>106</sup>

The same logic applies to non-ethnic regions as well. In particular, Stoner-Weiss’ (1997) case study of four *oblasts* in the early 1990s concludes that business elites in regions exhibiting higher degrees of economic concentration more readily overcame the collective action dilemma, forming into a cohesive interest group that “captured” the regional administration. In such cases, regional economic and political elites are bound by strong informal ties that facilitate an alliance providing steady rent-seeking channels to business elites and resource mobilization opportunities (primarily at election time) to politicians.

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<sup>105</sup> See, for instance, Stoner-Weiss, 1997; Andrey Schleifer and Daniel Treisman Without a Map: Political Tactics and Economic Reform in Russia (Cambridge, Mass: MIT Press, 2000), 90, 190-112, 140; Steven Solnick, “Russia’s Transition: Democracy Delayed, Democracy Denied?” Social Research 66:3 (1999): 789-814.

<sup>106</sup> See Treisman, “Russia’s ‘Ethnic Revival’” for a description of instrumentalist motives for assertion among the ethnic republics. This assertion is also based on interviews with Vasilii Fillipov, Center for Civilization and Regional Studies, Russian Academy of Sciences, Moscow, Fall 2001. A primary component of the ethnic republics’ drive for sovereignty in the early 1990s was securing control over major industrial assets and natural resources, and many of these regions used these rights to set-up regionally based companies. See chapter 5 for a more detailed discussion of this topic.

At the crux of this relationship are the large financial and administrative resources that are concentrated in the hands of a narrow circle of regional political and economic elites. As a result, tight-knit groups, akin to “cartels,” monopolize political and economic resources in the region, and are united in their desire to keep the competition – rival political and economic elites at both regional and federal levels – marginalized. Following from these observations, such patterns of cooperation and unity should also strengthen a region’s ability to assert the dominant elite alliance’s common interests vis-à-vis Moscow. Stoner-Weiss notes that wealthy regions with heavily concentrated industrial bases are better able to present a united front in bargaining with the center, which should fuel more assertive behavior.<sup>107</sup>

It is important, however, to distinguish between the size and structure of business actors and the level of government that they are primarily dependent upon for competing in Russia’s highly politicized economy. Theoretically, managerial elites in a region could generally divide along “national” and “regional” lines. The largest enterprises in a region that enjoy steady rent-seeking channels to the regional administration may also have influence on the national level, and may depend more heavily on the patronage of central bureaucrats to defend their business interests in the national market. Enterprise managers with national strategic interests would be less willing to rally around the flag of political and economic regionalism if doing so disrupts their relationships with federal patrons.

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<sup>107</sup> For instance, Stoner-Weiss found that certain regional governors could manipulate the center into better power deals by using natural resource wealth and industrial bases as bargaining tools. Stoner Weiss, 1997. Large-N analyses have also used aggregate measures of industrial and natural resource wealth as measures of bargaining power. See Treisman, 1997 and Dowley, 1998.

I argue that the political role played by Russia's largest businesses explains the dichotomy in regional behavior observed among the wealthy regions. When they control significant political and economic resources at the regional level, national-level businesses can enhance the central state's capacity to coerce and co-opt regional executives, acting as a constraint on assertive strategies despite strong instrumental incentives "from below." For regional political elites pursuing assertive strategies, regional-level enterprises can be an asset, but national-level businesses, which depend on steady channels to federal politicians, are a potential liability in a confrontation with the center because they can be a resource for the Kremlin. Moreover, in some regions national-level businesses act consistently as vertically-integrating mechanisms, structuring cooperation and reciprocity between federal and regional executives who depend on them for resource mobilization. Hence, my thesis ultimately rests on certain assumptions about the role of big business in the intergovernmental political arena, and these need to be outlined.

### **Big Business as a Natural Ally of the Federal Center**

Since the beginning of privatization in the early 1990s, the Russian economy has been dominated by an oligarchy of influential business structures, including a handful of metallurgical giants, vertically-integrated oil companies, gas and power monopolies, and Moscow-based financial-industrial groups (all of which are hereafter referred to as "national-level business," or "big business" for short).<sup>108</sup> Relying on an alliance with federal politicians and Moscow-based banks, they have consistently pursued strategies of

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<sup>108</sup> For a precise definition of national-level businesses based on size and structure, see Chapter 4.

vertical integration and consolidation of assets across the country.<sup>109</sup> While they are autonomous entities whose preferences clash repeatedly with federal objectives in fiscal and economic policy arenas (e.g. taxation, competition policy, structural reform), their strategic interests intersect with those of the Kremlin in two main respects.

First, national-level businesses rely on an “economy of scale” in the patronage they provide to federal officials who are willing to defend their interests in the national market.<sup>110</sup> For all big businesses, maintaining steady channels to federal decision-makers is vital for competition with rivals, especially for those that depend on the national transportation (e.g. oil and gas pipelines) infrastructure or that are primarily export-oriented.<sup>111</sup>

Second, the strategic alliance between big business and the center is based on a mutual aversion – the geographic fragmentation of Russia’s political and market space– that would inhibit the expansion of national business groups and at the same time undermine the Kremlin’s formal governance capacity. Widespread assertive regionalism would erode the state’s ability to coordinate the process of economic decentralization and ensure a uniform legal framework and infrastructure for the national market. In turn, a

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<sup>109</sup> Olga Kryshтанovskaya, “Finansovaya Oligarchiya v Rossii,” *Izvestia*, Jan 10, 1996; 5.

Kryshтанovskaya notes that the Kremlin has endeavored to manipulate the privatization process to create an “authorized class” of property holders that act as agents for the federal government in return for favorable treatment. By using the privatization process to consolidate Russia’s strategic assets in a narrow group of economic actors beholden to their patronage, Kremlin and government officials have ensured themselves steady access to financial, fiscal, and consequently political resources, while at the same time denying them to potential rivals in national and regional political arenas. Of course, just as happens on the federal level, regional governors have created their own “authorized classes” as bases of political and financial support that are independent of federal control.

<sup>110</sup> In particular, national infrastructure has been strictly controlled by the state, which gives the federal government a constant source of leverage over oil and gas companies that depend on state pipelines.

<sup>111</sup> See Yakov Pappe, *Oligarkhi, Ekonomicheskaya Khronika* (Gos.Un-t Vysshaya Shkola Ekonomiki, Moscow: 2000).

geographically fragmented market would raise the costs of doing business for national-level business actors. Indeed, assertive regionalism in Russia has often been accompanied by protectionism, various forms of economic populism and regional calls for greater state intervention in the economy to protect local industries.<sup>112</sup> Hence, for industrial groups expanding into a region, support from federal patrons is often vital for overcoming resistance by regional elites.<sup>113</sup>

Given their reliance on federal patrons and their aversion to national market fragmentation and regional protectionism, national-level businesses have a greater propensity to ally with the center.<sup>114</sup> In order to ensure a stable and predictable business environment, national-level businesses actors have an incentive to mediate intergovernmental conflict and deter assertive behavior that would threaten their relations with federal patrons. Moreover, in cases where national-level businesses have established a cooperative relationship with regional administrations, they can structure patterns of reciprocity between federal and regional politicians. There are various levers of influence national-level businesses have at their disposal to accomplish this, and these also must now be outlined.

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<sup>112</sup> See Chapter 3 for a detailed analysis of the agendas of various rounds of regional assertiveness. Many strategies were designed to give the regional government greater formal policy levers to intervene in the economy and reduce the “shock” of radical market reform, which often involved populist policies and redistribution of regional income to less productive industries.

<sup>113</sup> Pappe also notes that strong ties to federal officials are a significant bargaining chip for Moscow-based companies negotiating with regional politicians over the “rules of the game” within their jurisdiction.

<sup>114</sup> In the event of a conflict between a region and the federal center, the strategic interests of national-level businesses in the national or export markets would be most damaged by disrupting their relationship with federal rather than regional patrons. Regional governments can only offer businesses protection (e.g. a “krysha”) and legal guarantees within the borders of their respective jurisdictions.

## **Big Business as Sticks and Carrots**

The informal alliance between big business and federal politicians has meant that the “penetration” of national-level businesses in a region is often accompanied by an increase in the central government’s political leverage in that region. Local resources controlled by national businesses can be used both as “carrots” and “sticks” to co-opt or coerce regional politicians, respectively. For instance, when national-level businesses account for a large part of its tax base, a region is more vulnerable to various forms of fiscal manipulation by the central government. Special deals with key enterprises that bypass the regional administration can significantly undercut its tax collection capabilities.<sup>115</sup> Likewise, control over industrial inputs, such as energy and raw materials, gives national-level business much leverage over regionally-based industries.<sup>116</sup>

In particular, the takeover of strategic enterprises and their subsequent integration into national-level corporations and holding companies can undermine the power base of regional elites. The replacement of key managers and board members, coupled with corporate downsizing and restructuring, can disrupt corporatist arrangements between major enterprises and the regional administration, reducing governors’ control over the regional economy and straining social safety nets. Moreover, by supporting rival

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<sup>115</sup> Regional governments have also had to rely on the central government to mediate disputes over taxation and property rights with Moscow-based businesses, making political confrontation with the center more costly. The tax bases of wealthier regions still tend to be highly concentrated and dependent on a handful of major taxpayers. Interviews with economists at Raiffeisen Bank, Moscow, December, 2001.

<sup>116</sup> Besides state-owned monopolies, such as Gazprom and United Energy Systems, financial-industrial groups and oil majors have pursued strategies of buying up shares in regional coal and electricity companies, and are also moving into gas production and distribution as well.



politicians in the region – or even their own agents – in gubernatorial elections, national-level businesses have the potential to act as political sticks against incumbent governors. As will be demonstrated below, this has proven to be an especially effective strategy when accompanied with various forms of political pressure from the Kremlin.

National-level businesses also provide four types of economic “carrots.” First, their influence at the national level allows them steady access to federal decision-makers, which can bring a region federal investment funds and offer regional enterprises that integrate into the business in question fiscal benefits such as tax restructuring relief. Second, because of the high degree of concentration of financial resources in Moscow, these groups can generally offer substantially greater levels of private financing than are available internally in most regions. Third, they have helped integrate regional enterprises into both national and global markets. For regional enterprises, injections of outside financial resources and technical expertise, together with the presence of steady informal channels to federal decision-makers provided by national-level businesses, help ease the strain of adjustment to a market economy. Finally, national-level businesses can play an important role in financing social programs and development in the periphery.

Electoral alliances with national-level businesses can also be an important political carrot for regional executives.<sup>117</sup> Electoral alliances between an incumbent governor and big business are often cemented by networks of business and political elites that penetrate political and corporate institutions at both federal and regional levels.

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<sup>117</sup> See Vladimir Gelman, “Sub-national Institutions in Contemporary Russia,” in Neil Robinson, ed., *Institutions and Political Change in Russia* (New York, St. Martin’s Press, 2000). Especially in cases where the business is located outside of the region’s administrative center, it can effectively monopolize resources for political mobilization in its locality.

Federal and regional executives often serve on the boards of major corporations and/or their regional subsidiaries, which gives them a common interest in the company's performance. In most regions, national-level businesses have established a considerable presence in local legislatures, which can serve as an important political resource for the governor. Finally, national-level businesses have indirectly structured cooperation by supporting the expansion of national parties in the periphery. Alliances between national-level business groups and federal "parties of power" in a region are common, because both organizations are often beholden to the same patrons in Moscow.<sup>118</sup>

For regional elites, however, the political and economic carrots offered by national-level businesses come at a price. The greater the penetration of national-level businesses in a region's political economy, the more political and financial resources that they must essentially "share" with the owners of those businesses and, by extension, their federal patrons. Limiting the influence of national-level business actors in a region keeps political power more concentrated within existing regional-level elites. This, in turn, increases the region's relative bargaining power with the center, giving regional executives greater opportunities for pursuing "winner-take-all strategies" in order to maximize control over political and financial resources with their jurisdictions, with

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<sup>118</sup> The close relationship between business groups and pro-government/Kremlin sponsored parties was most vividly evidenced in the mid- to late 1990s by Prime Minister Chernomyrdin's "Our Home is Russia," which was closely associated with oil and gas companies and Moscow-based financial-industrial groups. Regional governors can take advantage of the resources already invested by national business groups simply by claiming affiliation with the "party of power" and contributing their administrative resources. Support of the national party of power by regional executives can bring rewards similar to those gained through more confrontational strategies. In the 1990s, regions that supported "Our Home is Russia" were invited to sign agreements alongside more assertive ones. Likewise, under Putin, concessions to Moscow mayor Yuri Luzhkov and Tatarstan President Mintimer Shamiyev, who were the main lobbyists for the repeal of an amendment limiting regional executives' terms in office, were reportedly linked to their support for the "United Russia" Party on the national level.

lesser fears of punishment in the next elections.<sup>119</sup> Conversely, when national-level businesses account for a larger portion of regional politicians' constituencies, they can use the various sticks and carrots at their disposal to raise the costs of assertiveness and increase the benefits of loyalty toward Moscow.

### **ACCOUNTING FOR THE MISSING VARIABLE**

I argue that models of regional strategic decision-making more fully explain patterns of assertive regionalism when the resources controlled by national-level businesses are taken into account. Without doing this, models based on socioeconomic structure tend to be overly deterministic. Based purely on aggregate measures of a region's wealth (e.g. levels of industrial output, export capacity, natural resource endowments) all the wealthy regions, whether ethnic or non-ethnic, are predicted to pursue assertive strategies. By distinguishing between the relative influences of national- and regional-level business actors, variations in assertiveness among regions with similar levels of economic incentives and political bargaining power can be better explained.

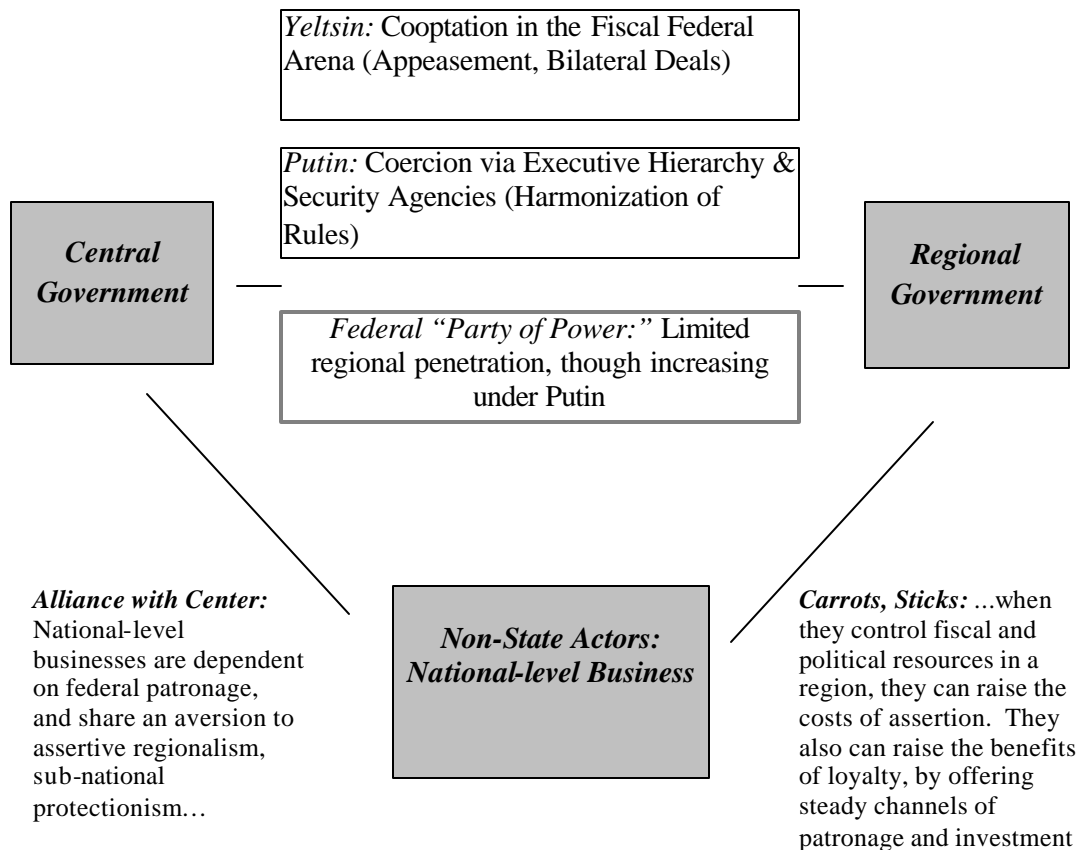
Likewise, state capacity approaches generally focus on the role of state actors and political institutions in the intergovernmental arena. I argue, by contrast, that the role of non-state actors must be taken into account as well, both as a political resource that enables the federal center to coerce and co-opt regional elites, and as a vertically integrating mechanism that structures reciprocities between regional and federal politicians over time. By forging informal strategic alliances with both federal politicians

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<sup>119</sup> Here I assume that regional executives would ideally prefer a "winner-take-all" outcome: retaining maximum control over the strategic enterprises in their regions.

and regional officials where their production assets are located, Russia's largest business actors have served as a "tie that binds" the post-Soviet federal state in an environment of weak state institutions and limited penetration of federal political parties at the regional level. Figure 2.1 depicts the strategies and mechanisms that have structured the dynamics of federalism in post-Soviet Russia.

Figure 2.1: Federal Strategies and Intergovernmental Mechanisms



## The Surprising Cohesiveness of the Russian Federal State

The thesis that big business has acted as a centripetal mechanism in the intergovernmental arena provides a different perspective on how the Russian Federation held together in the context of a weak central state. For instance, Treisman points to the federal center's ability to use selective incentives and manipulate the fiscal federal system in order to appease regions that presented the most credible threats to political stability and regime survival.<sup>120</sup> Treisman notes, however, that fiscal appeasement primarily benefited a narrow group of regions, primarily the larger "ethnic" republics, while it simultaneously drained federal coffers and diminished the state's capacity to "buy off" other regions.<sup>121</sup> Furthermore, it sharply raised the costs of federation for the majority of the wealthier regions that had to finance the government's largesse, increasing these regions' incentives for assertiveness. Fiscal appeasement, therefore, does not account for the loyal subset of wealthy regions. Instead, the influence of national level businesses in these regions helps to explain their restraint despite the relative unfairness of the fiscal federal arrangement during the 1990s.<sup>122</sup>

Big businesses' role as mechanisms of political integration reveals a view of state-business relations that is different from the one traditionally found in the Yeltsin-era

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<sup>120</sup> See Daniel Treisman, *After the Deluge: Regional Crises and Political Consolidation in Russia* (Ann Arbor: University of Michigan Press, 1999). Some scholars disagree that the federal center under Yeltsin even had the capacity to act strategically. See Stoner-Weiss, 1999.

<sup>121</sup> For a formal analysis of fiscal appeasement and how it progressively undermined the fiscal capacity of the federal government, see Daniel Treisman, "Political Decentralization and Economic Reform: A Game Theoretic Analysis," *American Journal of Political Science* 43 (April 1999): 549-517.

<sup>122</sup> Compared to fiscal appeasement (e.g. use of the federal budget for co-optation), big business can be viewed as a more efficient mechanism of distributing rents and co-opting assertive regions. It was less transparent, and thus did not incite protests, and also brought in outside financial resources for the federal government.

literature. While big businesses certainly have had a “horizontally” fragmenting effect on government at the federal and regional levels – by dividing the loyalties of government officials among competing financial-industrial groups – they also have played a “vertically” integrating role, enhancing the center’s capacity to constrain assertive regionalism. In this sense, the creation of Russia’s oligarchic capitalist system – which has been characterized by powerful rent-seeking business groups – represented a trade-off in the 1990s between the state’s formal extractive and regulatory capacity (tax collection, structural reform) and the political cohesiveness of the federal state.<sup>123</sup>

While Putin has demonstratively distanced himself from big business and emphasized the role of formal state institutions in regulating intergovernmental relations, there still have been major elements of continuity with the Yeltsin period in terms of the political role played by national-level businesses in the periphery. As the following chapters will show, fiscal and political centralization under Putin has tipped the scales in favor of big business at the regional level, further strengthening its influence in the periphery. As regions lose formal autonomy, they are less able to stave off “asset grabbing” by national-level business elites. Likewise, the regions’ diminished share of

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<sup>123</sup> This integrating function of national-level businesses reflects the important role that privatization can play in federal state building. “Spontaneous” privatization (which lacked any measure of political coordination from above) during the late 1980s and early 1990s expedited the breakdown of Soviet state hierarchies, whereas strategic privatization in the mid-1990s (which was heavily influenced by a narrow group of federal bankers and bureaucrats) strengthened the vertical integration of the nascent Russian Federation by partially reconstructing an economic hierarchy. In this sense, the “gathering of the assets” by national-level businesses under President Yeltsin was the first phase of reintegration, followed by the “gathering of the lands,” or strengthening of the formal state hierarchy, under President Putin.

fiscal resources in the consolidated budget has made governors even more dependent on the “carrots” provided by big businesses.<sup>124</sup>

## **CONCLUSION**

Conventional wisdom views Russia’s largest business actors as detractors from the central state’s governance capacity and as catalysts for assertive regional behavior. This chapter has presented a theoretical framework for viewing the top echelon of Russian companies – national-level businesses – as centripetal mechanisms, rather than centrifugal forces, inasmuch as they enhance the federal center’s political leverage over wealthy regions in an environment of weak formal state institutions and limited national party penetration in the periphery. Success in implementing federal strategy in both periods – decentralization via co-optation under Yeltsin and more coercive recentralization under Putin – has been greatest in regions where national-level business actors have maintained a strategic presence. The expansion of national-level businesses into the periphery and vertical integration of the country’s strategic assets has helped to build informal economic hierarchies that have supplemented formal political ones. The following chapters provide empirical evidence to support these claims.

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<sup>124</sup> In particular, the federal district system instituted by Putin has provided another venue for strategic alliances between federal officials and national-level businesses in the periphery. In fact, the relative power of major businesses vis-à-vis individual presidential representatives is greater than vis-à-vis the Kremlin, as there are less competitors for influence per access point: in many federal districts, only a couple national-level businesses dominate. The additional political leverage provided by national-level businesses also helps to explain patterns of success demonstrated by presidential envoys in compelling compliance with Putin’s mandate to abrogate bilateral agreements, both within and across federal districts.

### **Chapter 3: Center Periphery Conflict and Accommodation, 1990-2002**

This chapter provides a closer look at the dynamics of intergovernmental relations in general, and assertive regionalism in particular, throughout the Russian transition to democracy. Particular emphasis is placed on the wealthy regions that will be included in the regression analysis in Chapter 4. The chapter identifies a symmetrical pattern in the behavior of the wealthier regions across various configurations of formal and informal institutional factors, including variance in federal strategies and the strength of vertically-integrating mechanisms. In particular, two main themes serve as a common thread running through the first dozen years of the Russian transition.

First, despite variance in formal institutions and federal strategies, patterns of elite bargaining and accommodation primarily centered on the federal election cycle have persisted across the Yeltsin and Putin presidencies. Second, while the window for political opportunism stemming from central state weakness has gradually closed, the economic basis for assertive regionalism has remained constant throughout the entire period. As demonstrated in this chapter, regional assertiveness has been motivated by attempts to cope with the strains of sub-federal economic adjustment, in terms of either demanding more financial resources for protecting regional industries, or largely demonstrative, political protests to “pass the buck” and place the responsibility for social problems on Moscow's shoulders.

Within this overall pattern of continuity there has been considerable variation in the federal center's strategy toward the regions. The twelve year period from 1990-2002



can be divided up into three phases of intergovernmental relations. The first phase, from 1990-1993, encompasses the death knell of the Soviet Union (1990-1991) and the short-lived First Russian republic (1991-1993). During this phase, elite conflict at the federal level – between the newly-elected President Yeltsin and first Soviet leader M. Gorbachev, and then with the *ancien regime* parliament (Supreme Soviet) in 1993 – seriously weakened the center’s ability to enforce a consistent set of rules governing center-periphery interaction. As a result, this period was characterized by arbitrary rules and various unilateral actions aimed at widening a region’s political autonomy as well as a widespread “revolt” against the government’s fiscal stabilization and economic adjustment policies. In this phase, Russia’s wealthiest “ethnic republics” emerged as the pioneers of the regional autonomy movement, though many of the non-ethnic regions soon followed their example.

Yeltsin’s victory over the Supreme Soviet in October 1993 set the stage for the second phase, 1994-1998, which was inaugurated by the approval of a new Russian constitution and election of the first post-Soviet parliament in December, 1993. Although intense partisan divisions and ensuing executive-legislative conflict still curtailed the center’s ability to act as a united front vis-à-vis the regions, the Kremlin managed to contain regional assertiveness within a process of bilateral negotiations between federal and regional executives. Power-sharing treaties between the center and various regions, coupled with the institution of subfederal elections, enabled regional elites to formalize much of the autonomy that they had unilaterally “grabbed” in the first phase, while at the same time providing a framework for settling jurisdictional disputes. Political interaction

between center and periphery began to be “tamed,” while initial attempts were made to institutionalize Russia’s fiscal federal system. At the same time, conflicts over economic policy and the government’s persistent fiscal weakness sparked another revolt from below in 1996-1998, which peaked after the August, 1998 economic crisis, when the Russian Federation found itself on the brink of state breakdown.

The third phase, which began in 1999, has been characterized by both fiscal and political centralization. The political aftershock of the 1998 crisis led federal elites to coalesce around a strong central state, which was accompanied by the reemergence of Russia’s state security elites, or *siloviki*, who represent a powerful “stick” in intergovernmental relations after a decade of mostly “carrots.” As a result, regional assertiveness has been aimed at defending the formal autonomy achieved in the previous phase in the face of the center’s counter-offensive. This was first expressed in terms of political mobilization, specifically the building of political parties with strong regionalist agendas that united several of Russia’s wealthiest regions in opposition to the center’s bid to dismantle the asymmetrical federal system built in the 1990s.

However, after the defeat of the regional elite coalition to the Kremlin in the 1999 parliamentary elections, and the subsequent election of President Putin, regional assertiveness reverted back to its most typical form in the 1990s – with individual regions rather than coalitions as the main actors– although now it has taken on a distinctly defensive form. Instead of various types of revolts, ultimatums and declarations that characterized the Yeltsin regime, assertive regions have tried to “wait out” the center’s siege via a more passive form of defiance of federal objectives. Indeed, as the 2003-2004

election cycle drew nearer, the Kremlin increasingly evidenced the willingness to accommodate regional elites, resulting in a “two steps forward, one step back” pattern of centralization in Putin’s first term. The rest of this chapter delves into each of these three phases in more detail.

## **PHASE 1: FEDERAL FRAGMENTATION AND REGIONAL REBELLION**

### **1990-1991: The Parade of Sovereignties**

During the final years of the Soviet regime, many of Russia’s internal ethnic homelands, in particular the republics, followed the example set by the Union republics and issued declarations of sovereignty.<sup>125</sup> The “parade of sovereignties” from 1990-1991 represented the first strong impulse from below for democratization, decentralization and restructuring of the moribund federal system that Russia inherited from the Soviet Union. The ethnic homelands in turn set the example for the remaining regions, *oblasts* and *krais*, which followed suit in the proceeding years, demanding greater autonomy from Moscow. In this manner, the legacy of assertive regionalism that the Russian Federation inherited from the crumbling Soviet state was to define center-periphery relations for the next decade.

It is important to note that the drivers of the sovereignty movement within Russia itself differed in some ways from those precipitating the break-up of the Soviet Union.

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<sup>125</sup> As a republic itself in the Soviet federal system, Russia was further subdivided into administrative units (e.g. *oblasts* and *krais*) and “autonomous” ethnic regions (republics, *oblasts* or *okrugs*). The latter were distinguished as officially designated homelands of the titular nationality. The republics (hereafter referred to as “ethnic republics”) enjoyed privileged status in the ethnic region hierarchy as they were subordinate directly to Moscow, rather than a non-ethnic administrative unit. They also were the subject of central policies designed to promote an indigenous elite and were afforded some of the formal institutional trappings of autonomy. For further analysis, see Viktor Kozlov, *The Peoples of the Soviet Union* (London: Hutchinson, 1988).

Due to the demographic structure of Russia's historical ethnic homelands – titular nationalities constitute the majority only in a few regions, and in several cases are a minority – sub-national autonomy movements were not a mass popular phenomenon at the same level as in the most assertive constituent republics of the former Soviet Union, such as the Baltic States.<sup>126</sup> The presence of large Russian populations, coupled with rivalry among non-Russian populations, tempered the sovereignty aspirations of the most-independent minded republican leaders, while geographical constraints played a major role for non-border regions.<sup>127</sup> The influence of nationalist organizations has varied over time, and in many regions has waned since the earliest years of the transition.<sup>128</sup>

At the elite level, however, events on the national political stage in the early 1990s offered regional leaders a window of opportunity to assert control over political and fiscal resources within their territories. The threat of ethnic separatism proved to be a

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<sup>126</sup> For a comparative analysis of autonomy movements by the Soviet republics and the internal Russian republics, see, for example, Daniel Treisman, "Russia's 'Ethnic Revival': The Separatist Activism of Regional Leaders in a Post-Communist Order," *World Politics* 49:2 (1997): 212-249; and Philip G. Roeder, "Soviet Federalism and Ethnic Mobilization," *World Politics* 43 (January 1991), 197; Kisangani N. Emizet and Vicki L. Hesli, "The Disposition to Secede: An Analysis of the Soviet Case," *Comparative Political Studies* 27, no. 4 (1995).

<sup>127</sup> For a demographic and geographical analysis of Russia's internal republics, see Chauncy D. Harris, "A Geographic Analysis of Non-Russian Minorities in Russia and Its Ethnic Homelands," *Post-Soviet Geography* 34, no. 9 (1993). The presence of large non-titular populations constrained separatist aspirations by the titular nationality. For instance, Emizet and Hesli note that the concentration of the titular nationality is a significant predictor of the strength of secessionism in the Soviet case (p.530). Soviet policy toward Russia's internal Muslim republics, for example, encouraged divisions, such as the creation of a written Bashkir language (vs. the shared Tatar language) and the drawing up of borders and promotion of migration to include significant Tatar populations in Bashkiria, and vice-versa. Thus, not only Russians, but non-titular ethnic populations also increased the heterogeneity of many republics.

<sup>128</sup> For an account of the relationship between republican governments and indigenous nationalist movements in Russia's republics, see Michael McFaul and Nikolai Petrov, *Politicheskii Al'manakh Rossii* (*Russian Political Almanac*), Washington, DC: Carnegie Endowment for International Peace, 1998, especially the sections on Tatarstan and Bashkortostan.

salient bargaining chip in future dealings with Moscow.<sup>129</sup> Politically, popular elections that accompanied the sovereignty movements as early as June 1991 provided republican leaders, most of whom belonged to the Soviet *nomenklatura*, with an alternate, democratically legitimated base of power that put relations between regional executives and Moscow on a more even keel than that of their non-Russian neighbors, who could be fired on a whim.<sup>130</sup> In particular, the pioneers of the institution of regional elections were Russia's ethnic republics, including Chechnya, Tatarstan and Sakha-Yakutia, in addition to the cities of St. Petersburg and Moscow.

In terms of fiscal federalism, control over state property, tax revenues and natural resources were central issues in many of the republic sovereignty movements during this period, especially in the wealthier republics.<sup>131</sup> Following the example of the Union republics, some internal Russian republics halted regular tax payments to the federal center, instituting single-channel tax systems.<sup>132</sup> Other jurisdictional issues, such as citizenship, status of the titular language, control over the appointment of state officials in

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<sup>129</sup> Treisman, 1996 and 1999.

<sup>130</sup> The Chechen case is a notable exception that more closely mirrored developments in the Baltic states, where nationalist leaders replaced the Soviet ones in power during the onset of the autonomy movement. Otherwise, Soviet regional leaders (e.g. CPSU secretaries and other high-ranking members of the *nomenklatura*) have retained their positions in the lion's share of the internal Russian republics, much more so than in the non-ethnic regions. For a general analysis on elite continuity in Post-Soviet Russia, see John Higley & J. Pakalski, "The Persistence of Post Communist Elites," *Journal of Democracy* 2:133-147; Olga Kryshatanovskaya and Stephen White, "From Power to Property: The Nomenklatura in Post-Communist Russia," in Graeme Gill, ed., *Elites and Leadership in Russian Politics* (NY: St. Martin's Press, 1998).

<sup>131</sup> See for instance, Vera Tolz, "The Role of the Republics and Regions," *RFE/RL*, Vol 2, No 15, April, 1993; and Treisman, "Russia's Ethnic Revival."

<sup>132</sup> In its final years, the Soviet Union suffered from fiscal as well as political disintegration. The Baltic republics initiated a "tax revolt" by unilaterally revising rates of taxes remitted to Moscow, and eventually withholding all taxes. As other republics followed suit, state coffers were eventually emptied. Tatarstan and Chechnya were the pioneers in the Russian case; both republics unilaterally declared single channel tax systems in the early 1990s, ceasing payment into the Russian budget altogether for a period of time. See I. Demchenko, "Rossiyskiy Parlament Reshil Sam Soorudit Byudzhet v Piku MinFinu," *Izvestiya*, 10 July 1993, 2.

the region, etc. also dominated the ethnic republics' political agendas. As the ethnic republics also formed their own constitutions, many of which proclaimed the supremacy of republican over federal legislation, the stage was increasingly set for a "war of laws" that has plagued intergovernmental relations throughout the transition.

Moscow's reaction to the "parade of sovereignties" can be best summed up in Boris Yeltsin's oft-quoted exhortation to regional leaders to "take all the sovereignty you can swallow."<sup>133</sup> The newly elected president of the Russian Federation needed the political support of regional elites in his struggle with Soviet leader Mikhail Gorbachev for control over the Kremlin. While Yeltsin primarily had the more powerful ethnic republic leaders in mind, the leaders of Russia's non-ethnic regions (*oblasts, krays*) certainly weren't oblivious to the political window that opened up and the vulnerable position of the fragmented federal government.<sup>134</sup> In late 1991, the legislatures of various *oblasts* also began discussing the idea of upgrading their legal status in the Federation as well. Except for nationalist issues, their agendas were strikingly similar to those of the republics. During this phase, however, only a few *oblast* legislatures, such as Krasnoyarsk and Irkutsk, tested the waters by forwarding petitions to the Supreme Soviet to upgrade their status.<sup>135</sup> Unlike the ethnic regions, however, the *oblasts* refrained from unilateral declarations.<sup>136</sup>

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<sup>133</sup> *Berite stol'ko suvereniteta, skol'ko smozhete progлотit'!* The ethnic republics in particular proved to have a large appetite.

<sup>134</sup> For the sake of simplicity, the non-ethnic regions will be referred to as "*oblasts*." There has been no legal distinction between the status of *oblasts* and *krais* in either the Soviet or Russian system. The latter term tends to denote large border regions.

<sup>135</sup> "Will there be a Yenesei Republic?" *Current Digest of the Soviet Press*, Vol. 43, No.47 (1991), 24; and "Inner Soviet Adopts Resolution Asking Supreme Soviet to Recognize Irkutsk Province..." *Current Digest of the Soviet Press*, Vol. 43, No.47 (1991), 24. The governors of other regions such as Sakhalin also

## 1992-1993: Economic Adjustment and the Struggle for Equal Rights

The lowering of the Soviet flag over the Kremlin on December 25, 1991, heralded the short-lived First Russian Republic (1991-1993), which was increasingly plagued by rivalry between *ancien regime* institutions such as the Congress of People's Deputies and the newly institutionalized Russian presidency. The Soviet-era constitution and court system were ill-equipped to deal with the political realities of the transition, and just like the rivalry between Gorbachev and Yeltsin, the confrontation between Supreme Soviet Speaker Khasbulatov and Vice President Alexander Rutskoi on one side, and President Yeltsin on the other, kept the political window of opportunity open for assertive regional elites, who enjoyed a strengthened bargaining position due to their role as power brokers. Each side in the political conflict at the federal level was willing to accommodate regional demands in exchange for political support.

Just as significant as the mounting political paralysis on the federal level, in 1992 the federal government embarked on market reform, including price and trade liberalization, fiscal stabilization and a privatization program that was unprecedented in terms of its size and speed.<sup>137</sup> The federal government's economic policies had a significant impact on the regional autonomy movement during this period. Budgetary resources became scarcer, while natural resource rents became more valuable. This in turn thrust the issue of fiscal federalism – in particular the distribution of tax revenue, resource rents and economic policy authority – into the forefront of intergovernmental

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supported the idea of creating republics, but no resolutions were forwarded to the national parliament, as in the cases above.

<sup>136</sup> Oblast executives were appointed by the Kremlin until the institution of regional elections in 1995-97.

<sup>137</sup> Chapter 5 will take a closer look at the struggles surrounding privatization in center-periphery relations.

relations. At the crux of the issue was the viability of subjects of the Federation as autonomous political units based on the disposition of regional revenue and the redistribution of national income, as well as an independent sphere of expenditure discretion at the subnational level. The new Russian state had inherited a highly centralized fiscal system, where regions were considered administrative appendages of the state, and possessed virtually no formal budgetary discretion.<sup>138</sup>

While the republican sovereignty movement in 1990-1991 engendered a “war of laws,” the government’s stabilization program sparked a “battle of the budgets.” In the second quarter of 1992, the Ministry of Finance (MOF), in an effort to reduce the federal deficit and control hyperinflation, began to push expenditures for a wide range of social and public investment programs down to the regional level. Responsibility for expenditures for consumer price subsidies, cash subsidies for vulnerable groups, welfare programs for pensioners, family allowances, as well as various capital expenditures such as schools, hospitals, airports, highways, utilities, housing for military personnel and mandatory wage increases for public sector workers were transferred from federal to regional budgets. At the same time, the MOF imposed a hard budget constraint on regional leaders, ceasing the practice of adjusting tax-sharing rates to accommodate

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<sup>138</sup> Under the fiscal system inherited from the Soviet Union, subnational budgets were formulated in an administrative fashion by MOF in Moscow, and were always balanced, with the deficit at the federal level. Regional budgets had neither the legal right to raise their own taxes nor the ability to determine their own rates for shared taxes. There was no transparent, formula-based system to redistribute national income; instead, the new Russian government adjusted VAT tax deduction rates on a regular basis to meet individual regions’ budgetary needs (as determined by the MOF). In general, the process of centralized budget formation was plagued by many of the same types of problems as centralized planning: expenditure norms were often unreliable, and did not allow for sufficient flexibility or regional cost differentials. The ability of a region to finance desired programs depended mostly on its ability to lobby Moscow via informal channels. See A. Kalugin, “O Nekotorykh Problemakh Regiona’lnogo Upravleniya v Rossiiskoi Federatsii,” *Ekonomist*, No 8 (August 1993): 63-67.



additional expenditures. In essence, the government hoped to eliminate many of the social programs, and intended to “pass the buck” to regional administrations for the cutbacks.<sup>139</sup>

The legal vacuum in regard to Russia’s federal system in general, and the intergovernmental fiscal system in particular, exacerbated the situation. The absence of legislation authorizing regions to raise additional taxes and other sources of subnational revenue meant that they had to primarily rely on informal means such as lobbying to comply with the federal government’s mandates. A law on regional budgets intended to give regional officials more budgetary discretion passed by the Supreme Soviet in December 1991 was never realized, and as of mid-92 no legislation had yet been passed concerning the distribution of federal grants and transfers. The Federation Treaty, which was signed in March 1992, kept major issues, such as control over resources and taxation, open to future negotiations and legislation. Thus, regional leaders were essentially left to fend for themselves and compete with their neighbors for scarce resources and favorable deals with the federal center. Assertive regionalism – pressuring the center through declarations and threats – proved to be the most potent weapon in the macro-political arena.

The “first among equals” in this competition for resources were those ethnic republic leaders that had pioneered the sovereignty movement and had demonstrated the ability to mobilize resources to win elections in 1990 and 1991. Many of the most

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<sup>139</sup> As Wallich notes, Moscow aimed to absorb regional surpluses and shift the deficit downward from the federal to the regional level. Tax-sharing rates were set to force regional government to either cut back expenditures. At the same time, regions had little formal options for borrowing, so they were caught between a rock and a hard place. See Christine Wallich, *Fiscal Decentralization: Intergovernmental Relations in Russia* (Washington: The World Bank, 1992), 27-28.

assertive ethnic regions managed to secure special fiscal privileges in separate addenda to the Federation Treaty.<sup>140</sup> In addition, the republic of Tatarstan, which along with Chechnya refused to sign the Federation Treaty, held a referendum the same month on the question of formulating relations with the center via a bilateral treaty subject to international law. Armed with *vox populi*, Tatarstan, along with Chechnya, unilaterally instituted a single-channel tax system, sidestepping negotiation with Moscow.<sup>141</sup> All in all, a handful of Russia's wealthiest ethnic republics – Tatarstan, Chechnya, Bashkortostan, Sakha-Yakutia, Karelia and Komi – were able to assert control over a significant portion of the natural resources and fiscal revenue on their territories, either presenting the center with a *fait accompli* or negotiating extremely favorable deals.<sup>142</sup>

The growing asymmetry between the formal rights and fiscal privileges enjoyed by the ethnic republics and the limited autonomy of the *oblasts* (non-ethnic regions) became an increasingly politicized issue in 1992. Frustrated by their “second-class”

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<sup>140</sup> For instance, Bashkortostan was promised a fiscal scheme similar to a single-channel tax regime, whereby it retained well over ninety percent of its revenue and a large share of export revenue. Sakha-Yakutia and Karelia arrived at special deals whereby they could funnel their taxes through the federal budget and receive, respectively, 100 and 90 percent back. Komi managed a similar deal allowing it to retain 70-75 percent of its income. Sakha-Yakutia also received the right to retain a large share of proceeds of hard currency receipts and control over 20% of diamonds, 11.5% of gold. Bashkortostan was awarded 75% of its hard currency receipts. While some *oblasts* (Tyumen, Sverdlovsk), etc. successfully petitioned for more control over foreign economic activity and hard currency receipts (e.g. Siberian regions received 25%), none were awarded such special fiscal privileges (in terms of % of tax receipts kept in the regions). Vera Tolz, “The Role of the Republics and Regions,” and “A United States of Russia?” *Current Digest of the Soviet Press*, Vol 44, No.8 (92), 7-8.

<sup>141</sup> Moscow's refusal to allow Tatarstan to unilaterally implement a single-channel tax system (e.g. keep all of the revenue collected within the territory, and then negotiate with Moscow on the amount and timing of future tax deliveries) was a key issue motivating the republican leaders to refuse to sign the Federation Treaty and schedule the referendum. The success of the referendum was a strong bargaining chip in convincing federal authorities to “tolerate” the republic's fiscal separatism. See Ann Sheehy, “Tatarstan Asserts its Sovereignty,” *RFE/RL*, Vol.1 (14), 3 April, 1992, 11-4.

<sup>142</sup> Of these six regions, four were successful in effectively maintaining single-channel tax systems (or close equivalents) throughout the 1990s: Tatarstan, Bashkortostan, Sakha-Yakutia and Chechnya (Ingushetia as well after the division). Karelia and Komi were “cut off” in the mid-1990s. See Guboglo, 1997 and Lavrov, “Russian Fiscal Federalism: First Steps, First Results,” *Segodnya*, June 7, 1994, 5.

status and squeezed by the federal government's stricter fiscal and monetary policies, a number of *oblasts* in the Volga, Urals and Siberian areas of Russia launched a tax revolt in the summer of 1992, when their legislatures adopted decisions to revise revenue sharing with Moscow and effectively implement single-channel systems.<sup>143</sup> Among the reasons given by regional authorities for their act of defiance was the growing gap between federally-assigned expenditures and the amount of revenue left to the territories. Regional authorities were increasingly unwilling to spend their time in Moscow "sitting in waiting rooms and begging for allowances for their territories."<sup>144</sup> For instance, Chelyabinsk authorities bemoaned the fact that only 42% of the revenue generated in the oblast in 1992 remained in its budget, while it had to petition the MOF for loans in order to collect the harvest, implement federal conversion programs, finish nearly-completed construction projects and build housing for military personnel and migrants, in addition to meeting other social and capital needs. Similarly, Krasnoyarsk authorities decried the unfair redistribution of finances between the center and regions, claiming that it kept the *oblasts* on a short political leash.

Also included among Krasnoyarsk's grievances was the region's lack of control over the disposal of its resources, and the lack of compensation it received for their use. Krasnoyarsk Soviet Chairman Novikov cited the fact that while Buryatia, due to its privileged status as a republic, was able to pass a law on forestry, the oblast was not legally permitted to regulate the use of its forests or other resources, and thus could not

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<sup>143</sup> A.Orlov, "Preferentsial'niy Byudzheth Mog by Prekratit' Byudzhetye Razdory," *Ekonomika I Zhizn*, No 5 (February 1993), 5. Orlov notes that the unilateral actions taken by the regions were in protest to their "fleecing" (*obdiralovka*) by MOF.

<sup>144</sup> *Ibid.*

define its own economic policy.<sup>145</sup> Likewise in an article published in the summer of 1992, the head of Tyumen oblast, Yuri Shafrannik, complained that while oil and gas from the region accounted for over 60% of the Federation's hard currency receipts, the oblast as a whole occupied sixtieth place in terms of budgetary support for health, education and services. The Federation Treaty, Shafrannik asserted, remained only on paper – it was not observed by the MOF and supporting legislation had yet to be passed. Indeed, the title of Shafrannik's article, "A Strong Region Means a Strong Russia" summed up the concerns of many regional elites in terms of the discrepancy between their formal authority and that needed to effectively manage the tasks of economic adjustment and market reform.<sup>146</sup>

In contrast to its passive acceptance of the ethnic republics' assertiveness in the fiscal sphere, the MOF reacted swiftly to the uprising by the *oblasts*, employing various sanctions to force the regions to rescind their decisions.<sup>147</sup> At the same time, the Supreme Soviet, competing with the Kremlin for the loyalty of regional leaders, adopted legislation allocating regional governments discretion over at least 50 percent of their income, and pledged to support legislation to implement the Federal Treaty. Later, the Economic Council of the Supreme Soviet, in a report disseminated during the 7<sup>th</sup> Congress, recommended that the proportion of expenditures allocated solely to the regions be raised to 60 percent of the consolidated budget. However, the 1993 budget

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<sup>145</sup> Ibid.

<sup>146</sup> Yuri Shafrannik, "Sil'nyy Region – Sil'naya Rossiya," *Mezhdunarodnaya Zhizn*, No 8 (August, 1992), 30-35.

<sup>147</sup> Orlov, 1993. Among the sticks employed by the MOF were the freezing of export licenses and federally-funded programs, including the financing of "closed cities," and the denial of reciprocal credits to regional enterprises.

message delivered by President Yeltsin in January took into account neither the increased share of regional revenue enshrined in the legislation, nor the Economic Council's even more generous recommendations, instead offering only a marginal increase in revenue allocated to the regions.<sup>148</sup> The budget message sparked a wave of protest by regional officials in national newspapers, and during a meeting with the Supreme Soviet's Economic Council in March, *oblast* leaders complained that Moscow granted fiscal privileges to the republics "according to the measure of their national-separatist strivings," while discriminating against "law-abiding Russian oblasts."<sup>149</sup>

The federal center's intransigence, coupled with published reports of the fiscal privileges enjoyed by the ethnic republics, sparked another round of assertive regionalism in the summer of 1993, at an even broader level than the short-lived tax revolt during the previous summer.<sup>150</sup> In April, Chelyabinsk held an election for governor in defiance of Moscow. The federally appointed head of the administration refused to comply with the results, leading to a crisis of legitimacy in the regional government. Two *oblasts* – Vologda and Sverdlovsk – added a question onto the April 25<sup>th</sup> national referendum asking whether their regions should have the same rights as the ethnic republics, such as Tatarstan and Sakha-Yakutia, to which the majority of voters gave their approval. Armed

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<sup>148</sup> Ibid. The regions' overall share of the consolidated budget was scheduled to rise from 42.5 to 43.2 percent, while the share of expenditures was to rise from 30.0 to 32.8 percent, a far cry from the figures hoped for by the regions. The gap in regional financing often had to be made up by loans from the Ministry of Finance, which further exacerbated the region's dependence on Moscow.

<sup>149</sup> Cited in *Rossiyskiy Ekonomicheskiy Zhurnal*, No.3 (March 1993), 29-30. The letter of protest from regional leaders can be found in A Morozov, "Vlast' – Tsentru, Otvetsvennost' – Regionam," *Rossiyskaya Gazeta*, 20 January, 1993, 1-3.

<sup>150</sup> Data published in *Segodnya* newspaper, 25 June, 1993, 3, showed that the distribution of federal funds heavily favored the ethnic republics: of the fifteen regions which received more funds from the federal budget than they contributed, thirteen were republics.

with a public mandate, both regions proclaimed themselves as “republics” in the following months and began work on their own constitutions. Moreover, the governor of Sverdlovsk oblast, Eduard Rossel, extended an invitation to neighboring regions to join his region in forming a “Urals Republic” in recognition of the need for non-ethnic regions to enjoy the same economic and political rights as the ethnic republics.<sup>151</sup> In the ensuing months, the legislatures of several other regions adopted decisions to begin preparations (e.g. schedule referenda, formulate constitutions) for republic status, and officials in Tomsk and Irkutsk declared their intent to hold referendums on their respective region’s juridical status. Meanwhile, members of the Siberian Accord seriously debated whether or not to follow Sverdlovsk’s example and declare a Siberian Republic, which took place on the eve of the clash between Yeltsin and the Supreme Soviet.<sup>152</sup>

The decisions to adopt republic status stemmed from both economic populism and political opportunism. For instance, the decision of the Chelyabinsk legislature to hold a referendum on the issue of upgrading the region’s status (which ultimately did not take place) was partially motivated by the desire to dampen the effects of shock therapy, including price controls and the establishment of a higher minimum wage.<sup>153</sup> On the other hand, included with the elements of economic populism (which contained largely unfeasible policy prescriptions) was shrewd political calculation.<sup>154</sup> For regional

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<sup>151</sup> Chelikov, Vadim. “Respublika, Kotoroy ne Nuzhen Gerb,” *Moskovskie Novosti*, No. 31 (August 1993), A8.

<sup>152</sup> James Hughes, “Regionalism in Russia: The Rise and Fall of the Siberian Agreement,” *Europe Asia Studies* Vol. 46, No.7 (1994), 1133-1161.

<sup>153</sup> “Yet Another Republic,” *Current Digest of the Soviet Press*, Vol XLV, No.34 (1993), 24. German Galkin, “A President and a Tsar are Proclaimed Simultaneously in Chelyabinsk,” *Izvestia*, Aug 28, 2.

<sup>154</sup> For instance, freezing prices coupled with continuous wage increases. Even “red” regions such as Ulyanovsk were unable to maintain such islands of socialism for more than a couple years.

executives, the declarations also were part of assertive bargaining strategies aimed at extracting concessions from the center. In some cases they resulted in an immediate payoff to the region. For example, Maritime province, after an unsuccessful attempt to woo neighboring regions into a “Far Eastern Republic,” presented PM Chernomyrdin with a copy of a resolution adopted by the local legislature calling for a referendum to confirm the region’s status as a republic. The region then received permission to keep most of federal taxes that year.<sup>155</sup> In other cases, the payoff came later, in the second phase, in the form of the right to hold early elections (Sverdlovsk, Irkutsk, etc.) or maintain highly preferential fiscal regimes, as in the case of the most assertive republics (Tatarstan, Bashkortostan, Sakha-Yakutia, etc.)

Table 3.1 highlights *oblasts* that were most assertive of their political autonomy during this period, in terms of upgrading their status and holding referendums.

Table 3.1: Assertion of Formal Political Autonomy among the Wealthy Non-ethnic Regions, 1992-1993

	<i>Unilateral Upgrade of Status</i>
Executive declares “republic status”	Sverdlovsk, Vologda
Parliament adopts intent to declare, or supports interregional republic <sup>156</sup>	Altai, Arkhangelsk, Chelyabinsk, Irkutsk, Kemerovo, Khabarovsk, Krasnoyarsk, Maritime, Nizhny Novgorod, Sakhalin, Samara, Tomsk, Tyumen, Voronezh

<sup>155</sup> “Primorie Trebuyet Rasshirieniya Svoikh Prav,” *Izvestiya*, 2 September 1993, 4.

<sup>156</sup> The “South Urals Republic” was in fact declared in Chelyabinsk, but not by the chief executive who was officially the head of the regional administration. Instead, a contender in the gubernatorial elections in April 1993, who finished seventh, decided to take matters into his own hands and make the declaration in late July. The parliament did, however, adopt a decision to hold a referendum on the question, which never took place. It is included in this period as it represented the tail end of the “wave” of referenda begun by Tatarstan in March, 1992. The legislatures of Krasnoyarsk and Irkutsk first adopted a decision to petition the Supreme Soviet in late 1991; the idea of forming a joint (e.g. Enisey) republic was brought back to life

The most politically assertive oblasts during the summer offensive of 1993 were Sverdlovsk and Vologda, both of which officially declared themselves republics after holding public referenda.

While Prime Minister Chernomyrdin publicly denounced the *oblasts'* rebellion, the government, cautious of losing allies in its struggle with the Supreme Soviet, took no formal action at this point.<sup>157</sup> In August-September the regional rebellion further snowballed as it became increasingly clear that the government was not going to back down in terms of fiscal policy. Over thirty regions unilaterally withheld tax payments from the center which, coupled with the mushrooming “republic” projects, raised the specter of a Soviet-style state breakdown.<sup>158</sup> The explanations provided by *oblast* leaders for their assertiveness echoed the same concerns as the previous summer: their absolute and relative lack of autonomy.

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in summer, 1993. “Politicheskie Igri Vokrug Byudzheta,” *Moskovskie Novosti*, No. 28, 11 July 1993; Emel’yanenko, “Nastuplenie Provintsii na Kreml,” *Moskovskie Novosti*, No. 40, 3 Oct 1993, p.3A; and I Vetrov, “Ne Sliskom Dal’niy Vostok,” *Kommersant*, No. 33, 16-26 August, 1993, 18; “Vologda Province is Proclaimed a State within Russia,” *Current Digest of the Soviet Press*, Vol 45, No.20 (1993), 24-25; “More New Republics Loom; is Shakhrai the Loser?” *Current Digest of the Soviet Press*, Vol 45, No. 28 (1993), 6.

<sup>157</sup> V Chernomyrdin, “Ekonomicheskie Mery Pravitel’sstva – Platforma Natsional’nogo Soglasiya,” *Rossiyskie Vesti*, 7 August, 1993, 1-2. Chernomyrdin mentioned Rossel by name, who was later fired.

<sup>158</sup> Among the regions which threatened to withhold taxes were Krasnoyarsk, Altay Kray, Belgorod, Voronezh, Volgograd, Chelyabinsk, Sverdlovsk, Maritime and Khabarovsk Krays, Bashkortostan, Samara, Tatarstan, Sakha-Yakutia, Karelia, Udmurtia and all the “Golden Ring” *oblasts*. It was not a coordinated effort between all the regions, though most of the decisions occurred in the last week of August and first week of September, 1993. See R Batryshin, “Nalogovaya Voina Tsentra i Regionov: Boris Federov Ostupaet, Teryaya Milliardi,” *Nezavisimaya Gazeta*, 1 September 1993, 3.



The governor of Yaroslavl *oblast*, Anatoly Lisitsin, insinuated this danger in his explanation for his region's defiance:

“So long as one person is allowed to live at the expense of others and so long as Tatarstan spends everything only on itself and delays its dealings with other Russians, there will be no order. The epidemic of non-payments to the federal budget will end in a common grave.”<sup>159</sup>

In some individual cases, defiant regions were successful in coercing MOF into transferring additional funds to regional budgets. For instance, Yaroslavl authorities petitioned the MOF to keep 50% instead of 20% of VAT collections for a period of three months in order to offset the 8 billion ruble debt owed by the federal government to the *oblast*. The ministry refused, and it was only after the Yaroslavl legislature adopted the decision to withhold taxes that it was offered a three-month interest free loan, for the exact amount of the VAT deductions.

However, the rebellion did not have time to play itself out. Political events on the federal stage soon took precedence, as the constitutional crisis culminated in the shelling of the White House (which then housed the Supreme Soviet) by tanks friendly to President Yeltsin in the first days of October, 1993. Boris Yeltsin's victory over the Supreme Soviet brought an end to the political uncertainty on the federal level. By the end of the month the Kremlin had consolidated power and was able to turn its attention toward regional leaders. The government's response to the regional rebellion consisted of both “sticks” and “carrots.” In late October, Yeltsin issued an ukase authorizing the government to apply sanctions to regions not remitting the proper sum of federal taxes

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<sup>159</sup> Yu. Vakhnin, “Epidemiya Neplatezhey Zakonchitsya Obshchim Kladbishchem, *Rossiskaya Gazeta*, 17 September 1993, 4.

and authorizing the Central Bank to deduct the amounts from their current accounts.<sup>160</sup>

The federal government instituted a federal treasury system to reassert its control over the flow of tax payments from individual enterprises. In addition, Moscow cracked down on the most assertive *oblast* executives. Eduard Rossel of Sverdlovsk and Vitaly Mukha of Novosibirsk, chief architects of the Urals and Siberian republics, were fired, while the results of the unauthorized election held in Chelyabinsk were annulled.

At the same time, by way of concession, two of the most hard-line liberals, Yegor Gaidar and Boris Federov, were removed from their positions in the government.<sup>161</sup> The government stepped up its rhetoric on the need for equality among the regions, and several of the ethnic republics were forced to cough up tax funds that had been withheld during the previous quarters.<sup>162</sup> Despite intense lobbying by the ethnic republic leaders, the special legal status of republics as sovereign states was not formally recognized in the new Russian Constitution to the degree that it was in an earlier (July 1993) draft. Moscow also undertook efforts to meet regional demands for greater institutionalization of fiscal federal relations. President Yeltsin issued an edict establishing uniform VAT rates for 1994 and extending the right to regional and municipal governments to raise additional taxes and duties.<sup>163</sup> The edict also stated that in the future federally mandated

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<sup>160</sup> "On Measures for the Observance of Russian Federation Legislation and Budgetary Arrangements," signed October 28, 1993.

<sup>161</sup> Many regional leaders saw their removal as a "green light" for the further doling out of subsidies by the MOF. See V Tordes, "Gaidar and Federov kak Zakuska k Dotatsiyam," *Segodnya*, 22 January, 1994, 2; A Veslo, "S Otstavkoy Federova Pravitel'stvo Tatarii Spit Spokoinee," *Segodnya*, 28 January, 1994, 2.

<sup>162</sup> V Shirobokova, "Nalogovaya Voina Regionov s Tsentrom Ugrozaet Rossii Razvalom," *Finansovye Izvestiya*, 24-30 December, 1993, 2; D. Mikhaylin, "Idet Voina Byudzhetskaya," *Rossiyskaya Gazeta*, 22 Sept. 93, 3.

<sup>163</sup> "On the Formation of the Russian Federation Republic Budget and Its Relationship with the Budgets of the Federation Subjects in 1994," 6 January, 1994.

expenditures not agreed upon with regional governments would not be obligatory. In addition, the edict mandated the institution of a formula-based system for redistributing a portion of national income in order to smooth over the growing socioeconomic asymmetry among the regions. Finally, separate legislation allowed regional governments to share in federal tax room; for example, regions were allowed to set up a surtax on the federal profit tax rate.<sup>164</sup>

## **PHASE 2: FORMALIZING ASYMMETRICAL FEDERALISM**

The second phase of intergovernmental relations in Russia was inaugurated in December 1993 with the public approval of Yeltsin's Draft Constitution. There are three main areas of contrast from the previous phase. First, the adoption of a presidential system in the federal constitution formalized the supremacy of the executive branch, which solidified a form of intergovernmental relations akin to "executive federalism."<sup>165</sup> Bargaining amongst executives defined the rules of the game during this phase, and bilateral power-sharing treaties were signed with over half of the subjects of the Federation. Second, the institution of the Fund for the Financial Support of the Regions, together with tax-sharing principles enshrined in federal legislation, laid the formal foundation for a rule-based fiscal federal system better designed to address the needs of regional leaders in terms of sub-national economic adjustment. Third, the institution of regional elections nationwide strengthened the hands of regional executives vis-à-vis the center, changing the bargaining model from one of "principal-agent" to one of "principal-

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<sup>164</sup> G Cherkasov, "Nalogovoe Zakonodatel'stvo ne Postupilos' Printsipam," *Segondya*, 12 March, 1994, 2.

<sup>165</sup> For an excellent overview of the rise of presidentialism in Russia, and the problems associated with it, see Barany and Moser, 2001.

principal.”<sup>166</sup> Moscow’s ability to remove recalcitrant regional executives via fiat was curtailed, and electoral mandates became a potent bargaining chip in the intergovernmental bargaining game.

While the first phase was mainly characterized by unilateral actions designed to coerce the center into accepting regional autonomy projects as a *fait accompli*, assertive regionalism after 1994 was more confined to a process of bilateral negotiation. Federal elites were less disunited during this phase than during the previous one, and although sharp ideological divisions hampered executive-legislative relations, both the Duma – the new Russian parliament – and the Kremlin agreed on the general democratic rules of the game. Furthermore, the dominance of the Communist Party and other left-wing or nationalist groups in the 2d Duma – who are not known for their sympathy for the process of federalization – forced the regions to turn toward the federal executive branch for legitimization of their autonomy demands.

There were two separate streams of assertive regionalism in this phase: political and economic. The first began with a campaign by the ethnic regions to formalize their gains from the previous phase via bilateral power-sharing treaties with the center. Faced with a tough federal election cycle in 1995-1996, Moscow chose to selectively

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<sup>166</sup> See Richard M. Bird and Francois Vaillancourt, *Fiscal Decentralization in Developing Countries* (Cambridge, New York: Cambridge University Press, 1999.) and Richard Bird, “A Comparative Perspective on Federal Finance,” in K.G Banting, D.M Brown and T.J Courchene, eds *The Future of Fiscal Federalism* (Kingston: Queens University of School of Public Policy, 1994). The authors identify two types of models of center-periphery interaction in the fiscal sphere: the fiscal federal and federal finance models. The former is a “top-down” model based on the principal agent relationship. Here the federal government unilaterally sets the rules to maximize national policy objectives, such as economic growth, interregional equity, etc. The federal finance model emphasizes a consensual approach to fiscal decentralization that takes into account the political necessity of bargaining (e.g. principal-principal model) in order to account for geographical and ethnic diversity. When fiscal decentralization is accompanied (or preceded) by political decentralization, it is usually characterized by intergovernmental bargaining rather than delegation.

accommodate certain regions, in terms of both timing and substance, in order to gain strategic allies among the regional elite. An important result of this was the extension of the right to sign power-sharing treaties and hold regional elections to the *oblasts* in 1996. In the wake of the gubernatorial elections, the power struggle between regional and federal authorities gradually shifted from the political to the economic sphere. From autumn 1996 through summer 1998, certain regions launched a rebellion similar in agenda to the previous “tax revolts” of 1992-1993, but initially much more restricted in scope. The economic crisis that erupted on August 17, 1998, however, exacerbated the rebellion and brought the nation to the brink of state breakdown. The following section will look at each of these streams in turn.

### **Power-sharing Treaties and the Institution of Subnational Elections**

Russia’s wealthiest ethnic republics were the driving force behind the “contractual” style of federalism that characterized the treaty-signing process in the mid-1990s.<sup>167</sup> With the exception of Chechnya, the ethnic regions’ autonomy projects were not aimed at secession from the Federation. Instead, the republican elites aimed to secure a privileged status within the federation, in essence having their cake and eating it too. The Tatar “economic miracle” and prosperous situations in other republics amid the sharp economic decline in the country as a whole is a case in point.<sup>168</sup> Securing formal

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<sup>167</sup> Polishchuk, 2000 and Stoner-Weiss, 1999.

<sup>168</sup> In February 1994, the Prime Minister of Tatarstan, M Sabirov, boasted that because of its privileged fiscal status, Tatarstan was able to maintain the lowest prices for bread, milk and dairy products in Russia. Likewise, the Chairman of the Soviet of Ministers of Karelia, S Blinnikov, noted that the preferential share of hard currency receipts left to the republic allowed it to finance several major investment projects (e.g. railroad) and maintain an extensive welfare program, which, if not for the republic’s drive for economic sovereignty, would have been “unthinkable.” See M Sabirov, “My Vnosim Nalogi v Federal’ nuyu Kaznu:

recognition of their privileged status and property rights was a high priority for the leaders of resource-rich republics, such as Tatarstan, Bashkortostan and Sakha-Yakutia. By 1994, both Tatarstan and Bashkortostan had held successful referendums on the issue of defining relations with Moscow on the basis of a separate treaty governed by international law.<sup>169</sup> The republic of Tatarstan pioneered the agreement-signing process in February of 1994, when it concluded a treaty with Moscow delineating spheres of competencies over a wide range of jurisdictional matters. Bashkortostan and other ethnic republics soon followed suit. The treaty afforded the republics a wide range of autonomy in various spheres, and in effect legitimized their special legal and fiscal status as well as claims for control over natural resources and industrial assets on their territories. In particular, Tatarstan and Bashkortostan were able to bargain for virtually complete control over natural resources such as oil and the management of industries in the oil-processing and petrochemical sectors, while Sakha-Yakutia was assigned the lion's share of revenues from gold and diamonds.

For the federal government, the treaty-signing process allowed it to stabilize relations with the most assertive regional leaders and politically volatile regions. The outbreak of war in Chechnya was a glaring example of the consequences of the breakdown of the bargaining process.<sup>170</sup> In addition, the bilateral agreements provided

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no Summa Dolzhna byt' Real'noy i Obosnovannoi," *Nezavisimaya Gazeta*, 2 October 1993; S Blinnikov, "Nasha Tsel – Ekonomicheskii Suverenitet," *Delovoy Mir*, 28 Feb - 6 Mar, 1994, 14.

<sup>169</sup> Tatarstan was the pioneer of the referendum process (March, 1992); Bashkortostan added a question to the constitutional referendum in December, 1993.

<sup>170</sup> It also was an example of the potential for social upheaval and instability within a multiethnic region when a nationalist elite replaced the former Soviet one. Thus, Moscow has had a stake in accommodating the demands of the republican leaders who they can bargain with and whose goals are not nationalist/secessionist. In a sense, Moscow was "paying them off" to maintain stability in their regions

the federal center with more certainty regarding revenue collection. For instance, in exchange for a highly preferential tax sharing system, Tatarstan agreed to promise delivery of a fixed portion of the republic's revenue to the center. Moreover, the republic was assigned responsibility for financing various federal programs on its territory in exchange for the right to keep a larger share of revenue on its territory.

As soon as Moscow initiated the process of signing bilateral treaties with the republics, several *oblasts* began to clamor for equal treatment. For instance, in August 1994, the same month that the republic of Bashkortostan signed a highly preferential treaty with the Kremlin, the leadership of neighboring Perm *oblast* threatened to boycott President Yeltsin's Agreement on Social Accord unless it received formal rights similar to those of the ethnic republics – in essence employing blackmail tactics similar to those used by Tatarstan in 1992 when it refused to sign the Federation Treaty.<sup>171</sup> A delegation of officials from Perm followed up with a visit to Moscow, and, in addition to fiscal concessions, Perm received a promise that the treaty-signing process would eventually be extended to all regions.<sup>172</sup>

In general, the strategy of the most assertive regional lobbyists for “equal rights” focused first on holding regional elections and then negotiating with the center from a position of strength. Yuri Nozhikov, head of the administration of Irkutsk *oblast*, was the

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among the various ethnic groups. Interview with V. Fillipov, Center for Civilizational and Regional Studies, Russian Academy of Sciences, Moscow, Russia, May 2002.

<sup>171</sup> Bashkortostan signed a power-sharing treaty with Moscow earlier that month, and Bashkir President Rakhimov “rubbed it in” when he publicly boasted of the wide-ranging concessions he was able to wrangle from the Kremlin. Vladimir Todres, “So Far, Bashkiria is Pleased with the Sovereignty that it has Achieved,” *Segodnya*, August 7, 1994, 3. Leonid Nikitinsky, “Perm threatens Russia with a Divorce. The Blackmail Instrument is the Pact on Social Accord,” *Izvestia*, August 24, 1994, 1.

<sup>172</sup> Igor Labanov, “Moscow Promises Perm to Give Regions Equal Rights – Perm Promises to Participate in the Pact on Social Accord,” *Segodnya*, Aug 31, 1994, 2.

trailblazer, having won permission to hold a regional election in March 1994. Another outspoken proponent of the treaty-signing process, Eduard Rossel was granted permission to hold an election in August 1995, which brought him back to power in Sverdlovsk. Although by this time the Kremlin had already scheduled a general round of regional elections beginning in fall 1996, several other regional leaders successfully lobbied to hold their elections earlier, in December 1995.

In some regions, gubernatorial elections motivated regional executives to create their own “parties of power” on the local level. In Sverdlovsk, for instance, Eduard Rossel launched the “Transformation of the Urals” party, which had a distinct regionalist agenda aimed at securing greater economic autonomy and control over the region’s socioeconomic development. The party facilitated Rossel’s victory against the Kremlin-backed incumbent, and went on to give him a loyal majority in both houses of the region’s legislative assembly.<sup>173</sup> In contrast to other regional parties, Rossel’s movement also sent representatives to the national-level Federal Assembly, under the umbrella of the “Transformation of the Fatherland” party.<sup>174</sup>

Having prevailed over his Kremlin-backed opponent in the regional elections, Sverdlovsk governor Rossel spearheaded the bilateral agreement process, signing an agreement with Moscow in January 1996. Once the precedent was set, several other regions succeeded in signing power-sharing treaties with Moscow in the first half of 1996. The next round began a year after presidential elections in July 1997, and by

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<sup>173</sup> I. Barygin, ed. *Politicheskie Partii, Dvizheniya I Organizatsii Sovremennoy Rossii na Rubezhe Vekov* (St. Petersburg: Mikhailova V.A., 1999), 176-178.

<sup>174</sup> Ibid.



August 1998 over half of Russia's regions had signed treaties with the federal center. The defining feature of the treaty-signing process was the asymmetrical nature of the rights and responsibilities afforded to various regions. While Sverdlovsk's treaty afforded it a legal status almost equal to that of the republics, other treaties were more limited in the recognition of the political aspect of regional autonomy.<sup>175</sup> At the same time, many of the wealthier regions were able to negotiate the right to manage shares of state-owned enterprises, in order to gain more budgetary discretion and greater control over the regulation of mineral deposits and foreign economic activity.<sup>176</sup>

One of the main innovations of the treaties that benefited all the signatories was that a portion of federal taxes earmarked for financing federal or joint programs would remain in the regional branch of the federal treasury, instead of first going to Moscow. This was designed to allow more certainty in budgetary planning, since transfers from Moscow for federally and jointly financed programs were often delayed, or simply lost.<sup>177</sup> In many cases, regions were able to negotiate some sort of a regional investment fund based on retention of a certain share of tax receipts, export duties or other federal taxes. In addition, the treaties focused on specific geographical conditions and industrial sectors that were not being adequately addressed by federal policy.<sup>178</sup>

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<sup>175</sup> See V. Lysenko, "Distribution of Power: The Experience of the Russian Federation," *Conference Proceedings*, <http://www.ccpdc.org/pubs/moscow/html>. for a detailed analysis of Sverdlovsk's treaty.

<sup>176</sup> See for instance: Yelena Tregubova, "Irkutsk Province is another would-be Signer of a Treaty with the Center," *Segodnya*, Aug 5, 1995, 2. Andrei Chugunov, "Nizhny Novgorod Governor Chooses Money over Political Independence," *Kommersant-Daily*. Jan 18, 1996. 2.

<sup>177</sup> For instance, Kirov oblast was able to achieve a beneficial agreement on financing health care that resulted in more regular financing and improvements in efficiency. Interview with V. Reshetnikov, Kirov oblast administration, May 25, 2000.

<sup>178</sup> This was especially true of treaties with Bryansk (e.g. environmental and health problems associated with the Chernobyl disaster) Murmansk (which is located in the Far North), Kaliningrad (due to its unique

For Moscow, the decision to gradually accommodate the non-ethnic regions was greatly influenced by the federal election cycle in 1995-1996. The strength of opposition parties such as the CPRF and LDPR in 1993 parliamentary elections had demonstrated the saliency of the protest vote. First and foremost, the Kremlin was interested in securing the position of President Yeltsin against the Communist challenger, Gennady Zyuganov. Secondly, PM Chernomyrdin had a large stake in the success of the “party of power” – Our Home is Russia – in parliamentary elections. The privilege of holding an early election and being among the first agreement signatories was accompanied by the responsibility of “delivering the vote” for the federal government.<sup>179</sup> Thus, Moscow was first and foremost counting on receiving political dividends in exchange for satisfying autonomy demands from below.

The treaties signed with the *oblasts* also benefited the federal government fiscally. One of the most pressing problems in Russia’s fiscal federal system had been the lack of hard budget constraints on regional leaders. After the tax rebellion of 1993, the government took a more lax policy toward the regions in terms of enforcing fiscal discipline on the subnational level. Many regional deficits ballooned as regional governments showered generous tax privileges on politically important enterprises and resorted to barter and other monetary surrogates, while at the same time squeezing small businesses for cash. While encouraging a non-monetary economy that undermined federal tax collection, regional governors were quick to blame the center for under-

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geographical situation as an enclave in Europe), Buryatia (Lake Baikal) etc.. In the case of a treaty signed by the Kirienko government with Kemerovo, the lack of federal policy on restructuring the coal industry was the key issue. See V. Lysenko, “Distribution of Power: The Experience of the Russian Federation.”

<sup>179</sup> See Vladimir Popov, “Fiscal Federalism in Russia: Rules Versus Electoral Politics,” Working Paper, <http://www.nes.ru/public-presnetations/Papers/Popov.htm>, accessed on December 13, 2002.

financing regional programs and industries.<sup>180</sup> The treaties assigned certain responsibilities to the regional governments, in many cases with specific sources of financing generated within the region, making it more difficult for the governor to “pass the buck” to Moscow, a common game played by the regional elites trying to cover up their own fiscal inefficiencies and lax tax treatment of regional enterprises. Moreover, some treaties even negotiated mandatory decreases in regional deficits in exchange for other concessions.<sup>181</sup>

At the same time, third party enforcement of the agreements was particularly problematic. Until the summer of 1999, the State Duma refused to pass legislation to either regulate the treaty signing process or support any of the protocols enshrined in the treaties, while almost all the treaties violated the Constitution in one place or another, some more egregiously than others.<sup>182</sup> The sheer number of region-specific addenda and protocols made it difficult for government ministries to even keep track of their obligations, and each side lacked effective levers of control to consistently force the other

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<sup>180</sup> Regional governors were notorious for offering special tax privileges to large, politically important enterprises in their jurisdictions, often relying on non-monetary forms of exchange and elaborate systems of reciprocal credits, in addition to squeezing small businesses for live cash. The lack of live money in regional budgets has led to wage arrears of government employees and the under-financing of capital investment and social programs. Thus, it was easier for regional leaders to blame the center for underfinancing the regions, when in fact the high amount of monetary surrogates forwarded to the federal center (due to the lack of fiscal discipline at the local level) was a major problem. The Ministry of Finance asserted that a major cause of delays of budgetary transfers to the regions was underpayment to the federal budget. In addition, misappropriation of funds that are collected from regional enterprises has been a common problem at the subfederal level, in particular due to the lack of transparency in regional budgets. Therefore, regional budgets are strained partly because their leaders are unwilling to clamp down on regional enterprises or because the money, once collected, is misused. Interview with Arkady Dvorkovich, Ministry of Finance official, March, 1998.

<sup>181</sup> According to the agreement with Kemerovo, for example, the region had to reduce its 49 percent budget deficit by 13 percent and give the federal government 76 percent of the taxes and pension fund contributions collected in the region. In return, Moscow agreed to reduce the number of federal bureaucrats in the region and appoint regional representatives to 50 percent of the seats it holds on the boards of directors of regional firms owned by the federal government.

<sup>182</sup> See Stoner-Weiss “Central Weakness and Provincial Autonomy,” 1999.

into compliance.<sup>183</sup> Thus in some cases the agreements brought more in terms of political symbolism than consistent material benefits and budgetary certainty for regional elites. The simple fact of signing an agreement with the center was seen as a confirmation of the governor's ability to assert regional interests vis-à-vis Moscow. Many of them looked good on paper and were strong arguments during election time, and served to boost the governor's political stature among regional enterprise managers and the electorate.<sup>184</sup>

The following table identifies regions that negotiated power-sharing treaties with Moscow and held early elections during this phase. The timing of the event is an important indicator of a regional leader's preference intensity for the formal aspect of political and fiscal autonomy. Many of the most assertive regions were able to secure agreements and hold elections before the federal election cycle, when Moscow was in a more vulnerable position, and was more dependent on regional leaders to "get out the vote" in return for concession. Following presidential elections in 1996, the federal center took more control over the treaty-signing process and in most cases set its own timetable, as indicated by the gap from June 1996 – June 1997.

At the same time, negotiations with some of the more wealthy regions, such as Samara, Krasnoyarsk and Moscow City, began prior to the federal election cycle but dragged out into 1997 and 1998. Nevertheless, as indicated by the table below, some regions emerged as the pioneers of both the electoral and agreement signing processes within their respective cohorts. For the republics, these include Tatarstan, Sakha-Yakutia

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<sup>183</sup> Interview with V. Reshetnikov, Kirov oblast administration, May 25, 2000.

<sup>184</sup> Interview E. Volkova, Soviet Federation Apparatus, March, 1999. Volkova noted that the difference between what was offered a region on paper and what was actually received was significant, especially due to difficulties in federal revenue collection and mounting internal debt payments in the latter 1990s.

and Bashkortostan; among the oblasts, Irkutsk and Sverdlovsk pioneered the drive for regional elections and bilateral treaties. At the same time, several of the wealthier *oblasts* did not sign treaties with the federal center at all, including Tyumen, Tomsk and Lipetsk.

Table 3.2: Wealthy Regions' Elections and Bilateral Treaties

<i>Timing (In relation to 1995-1996 federal election cycle)</i>	<i>Regional Elections (oblasts only)</i>	<i>Power-Sharing Treaty (all regions)</i>
<i>Prior ( 2/94 - 8/95)</i>	Irkutsk, Sverdlovsk	<i>Republics</i> of Bashkortostan, Sakha-Yakutia, Tatarstan, Udmurtia
<i>During (12/95 - 6/96)</i>	Belgorod, Moscow Oblast, Nizhny Novgorod, Novosibirsk, Maritime, Omsk, Orenburg, St Petersburg, Tomsk, Tver, Yaroslavl, and others	<i>Republic</i> of Komi; <i>Oblasts</i> : Altai, Irkutsk, Khabarovsk, Krasnodar, Leningrad Oblast, Nizhny Novgorod, Omsk, Orenburg, Perm, Rostov, Sakhalin, St Petersburg, Sverdlovsk, Tver
<i>After (9/96+)</i>	Remainder of <i>Oblasts</i>	Cheliabinsk, Kirov, Krasnoyarsk, Moscow, Murmansk, Samara, Saratov, Ulyanovsk, Vologda, Voronezh, Yaroslavl, and others

### **The Center's Fiscal Offensive and the Regions' "Economic Revolt"**

One of President Yeltsin's first moves after his reelection was an attempt to revive the state's deteriorating financial situation. Anatoly Chubais took the helm of the Ministry of Finance and launched a campaign to rein in errant taxpayers.<sup>185</sup> Most

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<sup>185</sup> Chubais formed the Temporary Extraordinary Commission on Strengthening Tax and Budget Discipline; the first part of the name of the committee was the same as that of the Bolshevik committee in charge of state security in the years immediately following the revolution.

significantly for the regions, in 1997 the MOF began to regularly sequester federal expenditures in an effort to trim the mounting federal deficit.<sup>186</sup> The cutbacks affected articles in the budget for regional investment and social programs, funds through the Fund for Financial Support to the Regions, as well as extra-budgetary funds. In addition to outright sequestration, delays in transfers to the regions became commonplace, and the federal center was often unable –or unwilling – to live up to its side of the bargain contained in the bilateral agreements.<sup>187</sup> Chubais also promoted a plan to divide Russia into federal tax districts in an effort to dilute some of the regional leader's influence over budgetary flows, and also to broaden the authority of presidential representatives in the region over federal ministries, many of which were de-facto under the control of regional administrations that paid their salaries.<sup>188</sup>

While the federal district idea never materialized, the sequestration of the federal budget represented a threat to regional finances similar to that during the onset of fiscal stabilization in 1992-1993. In addition, by now several years had passed and the country was still suffering a decline in many sectors of industry. Increasingly frustrated by Moscow's inadequate role in the economy and unilateral budgetary cutbacks, regional executives began to take matters into their own hands. In the fall of 1996, Omsk governor Leonid Pozhelyaev launched a new round of regional protests by challenging a presidential decree giving the Ministry of Finance extraordinary powers to punish

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<sup>186</sup> The government had to cut one-fifth of the planned expenditures in the 1997 budget due to a revenue shortfall in the first quarter.

<sup>187</sup> See fn. 60.

<sup>188</sup> In Kirov oblast, for instance, the presidential representative's office was understaffed and unable to keep up with its duties. The regional administration staff de-facto assumed many of the presidential representative's responsibilities. Interview with V. Reshetnikov, and other staff members, Kirov oblast administration, May 25, 2000.

enterprises not remitting their taxes on time. Pozhelyaev, together with regional defense enterprise managers, effectively issued an ultimatum to the center, claiming that if it did not remit 2.5 trillion rubles owed to industries and state workers in the region, Omsk and other Siberian provinces would be forced to take matters into their own hands.<sup>189</sup>

It is important to note that Omsk authorities cited the center's ineffective regional policy as one of the main reasons for their protest, complaining that the federal government relied exclusively on informal channels (e.g. patronage) for dealing with regional officials and only tried to "put out fires" – waiting until crises occurred before addressing pressing needs. While the immediate pretext for Omsk's assertiveness was the center's attempt to flex its muscles and clamp down on regional taxpayers, survey data indicates that the root of the problem for regional elites across Russia actually lay in the center's fiscal and economic policy weakness.<sup>190</sup> This same theme was sounded in similar ultimatums in February 1997 by Maritime Province governor Yevgeniy Nazdratenko and Sverdlovsk governor Eduard Rossel. Rossel, who represented the Association of Urals executives, gave the government several weeks to come up with a sound industrial policy.<sup>191</sup>

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<sup>189</sup> While the regional protest began as a march organized by local defense industries, governor Pozhelyaev played an instrumental role in translating the spontaneous act into an ultimatum directed against the federal government. See Vladimir Golubev, "Counter-Offensive Against Moscow: Regions Answer the VChK's Demand for Payment of Taxes by Issuing Ultimatum," *Trud*, 21 November, 1996, 3.

<sup>190</sup> According to an elite survey conducted by the Russian Academy of Sciences, the majority of regional elites complained that they were forced to take matters in their own hands because of the federal center's lack of effective regional and industrial policy, the poor tax system, and the lack of coordination between federal and regional bureaucracies. "*Rossiya: Tsentri i Regiony* (Russia; Center-Periphery Relations)" No.2, Institute for Sociopolitical Research (Moscow: Russian Academy Sciences, 1998), 99.

<sup>191</sup> Viktor Ivanov, Viktor Smirnov and Denis Dyomkin, "Eduard Rossel Gives Moscow until February 20; Urals and Maritime Territory Stage Economic Revolt," *Kommersant-Daily*, Feb 6, 1997, 2.

In additions to ultimatums, several “tax revolts” took place during this time period. In February 1997, the Sakhalin legislature voted to withhold taxes from Moscow in retaliation for the Kremlin’s failure to meet its fiscal obligations in the region. When challenged by the government, the oblast governor, Igor Fakhrutdinov, supported the regional legislature, though he convinced it to revoke the decision the following month after the federal government paid off some of its debt. Likewise, Irkutsk governor Vitaly Nozhikov launched a short-lived tax rebellion in March, citing that the federal budget’s debt to the region had swelled to two trillion rubles, while it had forwarded twice that amount to federal coffers for 1996. An Irkutsk delegation arrived in Moscow to negotiate right after the oblast’s announcement, but apparently left empty-handed.<sup>192</sup> Three days later, the Finance Ministry and Prosecutor General’s Office forced him to cancel the decree. Other regions, such as St Petersburg, Tula and Krasnodar, and later Krasnoyarsk, followed suit with threats of tax withholding for similar reasons, often to little or no avail.<sup>193</sup> The protests did have political significance, however, in redirecting the ire of regional enterprises and electorates from regional to federal authorities, in essence “passing the buck.”<sup>194</sup> Another major theme of regional protests during this period was

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<sup>192</sup> Dmitry Kamyshev, “Irkutsk Secedes From Russia...for a Month, at least,” *Segodnya*, March 4, 1997, 1. Dmitry Kamyshev and Irina Nagomykh, “Irkutsk Governor’s Tax Revolt is Put Down,” *Segodnya*, March 5, 1997, 1-3.

<sup>193</sup> Irina Nagornykh, “Politically Condemned Prisoners Fall in the Budget Gap: the Regions’ Tax Rebellion becomes Nationwide,” *Segodnya*, March 6, 1997, 3. “Kremlin Succumbs to Blackmail,” *Current Digest of the Soviet Press*, Vol 50; No.18 (1998), 14. Krasnoyarsk was apparently more successful in coercing the government to pay of a 50mln ruble debt in May, 1998, as leaders also threatened to hold a referendum on the region’s political/legal status in the Federation.

<sup>194</sup> Interview with E. Volkova, Soviet Federation Apparatus, March 1999. Assertive regionalism was as much a political game as a battle for control over concrete economic and fiscal resources (which also had political significance in that they allowed the governor to increase the scope of rent distribution).



the special rights and privileges enjoyed by the ethnic republics, which had also figured prominently in the 1992-1993 rebellion.<sup>195</sup>

Ultimately Yeltsin's attempt to restore the state's fiscal capacity failed, and the swelling deficit forced the government to default on its internal debt obligations in August 1998, triggering an economic crisis that forced the government to resign. During the five-week interregnum, the federal center effectively lost all levers of control over the regions, and speculation of state breakdown into a confederation again dominated the headlines.<sup>196</sup> The outbreak of regionalism during the first several weeks of the crisis differed from prior rounds of regional defiance in that it was more a function of self-preservation, and not directed at bargaining with the federal center. As such, it was more closely linked to outright autarky rather than the previous patterns of assertion followed by negotiation.<sup>197</sup> Nevertheless, even after the new government of Yevgeniy Primakov came to power, several regions continued to delay payments or declared new "tax revolts," including Khabarovsk and Omsk, citing traditional grievances.<sup>198</sup>

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<sup>195</sup> For instance Krasnoyarsk governor Zubov, during a meeting between Chubais and the Siberian Interregional Association, warned that if the federal government did not stop giving preferences to such regions as Tatarstan, Bashkortostan, Sakha, Moscow, and Ingushetiya, it could no longer count on the support of the Siberian governors. See "Chubais Brings Budget Woes to Siberia," *Russian Regional Report*, 02/17, 15 May 1997.

<sup>196</sup> Regional responses included the declaration of state of emergency and formation of emergency committees with wide-ranging powers over economic activity in various regions, decisions to create gold/hard currency reserves, price controls, restrictions on goods imported and exported to other regions, etc. For a more complete overview: See Sledzevsky, I.V., "Regionalism in the Russian Federation as a New Socio-cultural Reality" in *Federalism and Regional Relations* (Moscow: Ethnosphere, 1999).

<sup>197</sup> See especially Gail Lapidus, "Asymmetrical Federalism and State Breakdown in Russia," *Post Soviet Affairs*, 15 (January, 1999):74-82.

<sup>198</sup> Tomsk had suspended tax payments immediately after the crisis, but resumed after negotiations with the new Primakov government. The rationale given for revolts after the new government was formed was less due to a crisis situation and more typical of past actions, e.g. repayment of federal debts to the region. Pyotr Akopov, "Fate of United Russia depends on Regional Leaders," *Nezavisimaya Gazeta*, Sept 24, 1998, 1.

### PHASE 3: CENTRALIZATION AND HARMONIZATION

The third phase of intergovernmental relations is distinguished by a marked trend of political and fiscal centralization. The August 1998 crisis reinforced the dangers of excessive decentralization and triggered the realignment of both federal and regional elites around the necessity of strengthening the central state, while the fall of the Chernomyrdin government paved the way for improvements in executive-legislative relations that culminated in the Kremlin's pact with the Communist opposition after Putin's victory in presidential elections. Indeed, the laissez-faire "Chernomyrdin" model of intergovernmental relations, which was built solely on central accommodation of regional demands in exchange for political favors, proved inadequate to deal with the nationwide problem of economic adjustment and also failed to generate any lasting measure of political consensus from below.<sup>199</sup>

The assertiveness of the federal center structured two major changes that have affected patterns of regional behavior. First, the political window of opportunity for regional elites to formally expand their autonomy has largely closed. Whereas before assertive regional governors could play on divisions in the center, since 1999 the federal center has more or less acted as a united front vis-à-vis regional elites.

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<sup>199</sup> For instance, surveys and interviews with regional leaders conducted in 1997-1999 show that issues of asymmetry and perceptions of unfairness were among the most salient for regional elites in the *oblasts*. V. Fillipov and D. Grushkin, *Federalism Kak on Est* (Moscow: East-West Institute, 2001), 124-218; and *Rossiia: Tsentr i Regiony*, 1998.

Second, a united center has been much more active in generating legislation to structure the rules of center-periphery relations, and the collective bargaining process that takes place in parliament leaves much less room for asymmetry – e.g. special privileges and rights afforded to a narrow subset of regions – than the bilateral style of executive federalism that dominated the mid-1990s. Indeed, in 1999 the federal center began to harmonize intergovernmental fiscal relations, and these initial efforts grew into a concerted campaign in 2000-2002 to take back many of the privileges that were handed down during the Yeltsin years and reassert central control over executive agencies in the periphery.

This phase can be divided into two periods. The first, 1999, was a transitional year centered around the federal election cycle (parliamentary elections in December 1999 and presidential elections in 2000). In this period assertiveness was expressed as a collective effort on behalf of a privileged group of executives who built and/or supported regionalist political parties to defend their particularistic interests at the national level. Their decisive defeat in parliamentary elections to the Kremlin's new "party of power" effectively doused any hopes of turning back the tide of political centralization. The second period began in summer 2000 when President Vladimir Putin launched his plan to reengineer the entire system of intergovernmental relations "from above." Assertiveness reverted back to its most typical form in the 1990s – with individual regions rather than coalitions as the main actors– although now it took on a distinctly defensive form. Instead of various types of revolts, ultimatums and declarations that characterized IGR under the Yeltsin regime, assertive regions have tried to "wait out" the

center's siege via a more passive form of defiance of federal objectives. Indeed, patterns of compliance to President Putin's mandate to do away with the bilateral power-sharing treaties indicate a clear difference between loyal and defiant regions.

### **1999: Political Uncertainty and Regional Mobilization**

By January 1999, the Primakov government had finally put together an anti-crisis program. Economically, the government favored greater state intervention, while politically, a number of major reforms in Russia's federal system were suggested. These included doing away with the institution of subnational elections and appointing governors from Moscow, combining regions into large aggregates, and drawing up legislation to remove governors from office for direct violations of the constitution. At the same time, Primakov exercised various "carrots", such as bringing regional governors into the Cabinet and resigning the bilateral power-sharing treaty with Tatarstan in February 1999. The "sticks," however, were never implemented, as President Yeltsin sacked Primakov in May of that year.

The next two prime ministers, Sergei Stepashin and Vladimir Putin, were recruited from the ranks of Russia's security ministries, as the Kremlin attempted to draw upon other institutional resources and elite groups to rein in both regional and business elites.<sup>200</sup> Indeed, 1999 witnessed the beginning of a trend of increased activity by the Prosecutor General's Office and the Federal Security Service (FSB) in the regions, foreshadowing President Putin's more heavy-handed approach in the intergovernmental

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<sup>200</sup> Stepashin was head of the Ministry of Internal Affairs, and Putin head of the Federal Security Service prior to their appointments.

arena. Two other key developments also set the stage for the following period. First, the Ministry of Finance began an overhaul of the country's fiscal federal system in order to optimize revenue and expenditure assignments across levels of government. This gradually entailed a general revision of revenue sharing rates in favor of the federal government, as well as phasing out of special privileges for the ethnic republics.<sup>201</sup>

Secondly, for the first time in Russia's transition, executive-legislative relations began to normalize, at least between the Cabinet and the Duma.<sup>202</sup> This enabled the government to finally begin pushing through legislation governing intergovernmental relations, and in particular to begin overhauling the Tax Code. A landmark piece of legislation passed in 1999 mandated that all bilateral power-sharing treaties had to be brought into conformity with the Russian Constitution and federal legislation or be annulled by July, 2002. This was the federal government's first real attempt at asserting its legislative supremacy and harmonizing the legal status and rights enjoyed by the federation's constituent units.

With the storm clouds of centralization forming on the horizon, regional governors scrambled to position themselves for the upcoming elections. 1999 witnessed an unprecedented burst of party building by regional leaders due to two main factors. First, Yeltsin's popularity hit its nadir after the crisis, and more politically ambitious regional elites such as Moscow mayor Yuri Luzhkov and Samara governor Konstantin Titov were eyeing the Kremlin. A strong showing in parliamentary elections would be a

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<sup>201</sup> Leonid Smirnyagin, "Russian Federalism: Paradoxes, Contradictions and Preconceptions" in *Federalism and Regional Relations* (Moscow: Ethnosphere, 1999), 37-40.

<sup>202</sup> The inclusion of Communist politicians in the Primakov and following governments did a lot to ease tensions between the Cabinet and the Duma in 1999.

vital boost for the presidential campaign the following summer. Indeed, in early 1999 both Luzhkov and Titov launched their own parties. Titov's Voice of Russia proved to be an unsuccessful attempt to reconstruct Chernomyrdin's "Our Home is Russia," and it soon collapsed under the pressure of political rivalry.<sup>203</sup> Luzhkov's Fatherland party was more successful, and included several core members from larger regions such as Nizhny Novgorod and Moscow Oblast.

The second motivation for political mobilization was an attempt by regional elites to defend their autonomy on the national political stage. Luzhkov is known for his authoritarian leadership style, and his party's platform has a distinct unitary bent.<sup>204</sup> Regional leaders feared that he would overturn the status-quo (in particular regarding privatization) and attempt to rescind some of the privileges that they had gained over the past decade. In response, the presidents of Tatarstan and Bashkortostan, joined by St Petersburg governor Yakovlev, launched the "All Russia" party, which has a very strong regionalist agenda. On the eve of the 1999 elections, the party's platform included proposals to increase the fiscal autonomy of regional administrations and to allow them more control over personnel decisions in their regions. Additionally, the party's platform called for reforming Russia's electoral system in order to eliminate party-list seats in the Duma, since regional executives have much more control over the prospects of single-mandate deputies.<sup>205</sup> A key feature of the All-Russia party is that it placed Russia's wealthiest ethnic republics and *oblasts* on the same side of the fence. While previously

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<sup>203</sup> Oleg Petrovich Kudinov, *Osnovy Organizatsii I Provedeniya Izbiratel'nykh Kampanii v regionakh Rossii*, (Kaliningrad: Yantarniy Skaz, 2000), 58.

<sup>204</sup> Barygin, 1999, 115-118.

<sup>205</sup> Ibid.

assertive *oblasts* had led the struggle for “equal rights” with the ethnic regions, by now many of them had secured special privileges of their own, and found themselves in the same camp as the republics in defense of the status-quo.

In response to the wave of political mobilization from below, the Kremlin launched its own party, Unity, which enjoyed the patronage and active support of many federal government officials. In stark contrast to All Russia, which appealed to richer regions, Unity actively courted poorer regions, promising greater fiscal centralization, and, accordingly, more federal transfers and subsidies. In particular, Unity played on the theme of asymmetry in Russia’s federal system, calling for greater equalization. As Unity became increasingly successful in garnering support, the leaders of Fatherland and All Russia decided to join forces and run on the same ticket. Luzhkov and Shamiyev successfully courted former PM Primakov as the party’s presidential hopeful.

### **2000-2002: Central Consolidation and Regional Resistance**

The victory of the Kremlin’s “party of power,” Unity, in December parliamentary elections dealt a serious blow to both the “Fatherland-All Russia” movement as well as the presidential aspirations of its leaders. The solidarity evidenced during the election campaign by the majority of Russia’s wealthy regions quickly dissolved in early 2000, as most regional leaders quickly acquiesced to the Kremlin and threw their weight behind PM Vladimir Putin’s presidential campaign.<sup>206</sup> Not soon after Putin’s victory, Fatherland-All Russia and Unity formed a coalition in the parliament, dashing any hopes

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<sup>206</sup> Some governors caved in sooner than others: Cheliabinsk governor Sumin, a key supporter of All Russia, went over to the Unity camp only two weeks after parliamentary elections.

that All-Russia leaders might have had of forming a party in the parliament that would seriously challenge the Kremlin in defense of regional autonomy. Accordingly, in the summer of 2000, the governors' fears of centralization and harmonization were justified as Putin embarked on a wide-ranging overhaul of Russia's federal system.<sup>207</sup> Many of Putin's initiatives, such as the centralization of the fiscal system, removal of governors from the Federation Council and the institution of the federal district system now met with little organized resistance except for vocal criticism from disgruntled regional leaders.

When it came to wrenching back autonomy from individual regions, however, the Kremlin encountered sporadic acts of regional defiance, in particular regarding its reassertion over personnel decisions in federal agencies.<sup>208</sup> The most difficult task for the center thus far, however, has been implementing the 1999 law mandating that the bilateral power-sharing treaties be either rewritten or annulled. Due to the juridical status of the treaties, they cannot be unilaterally abrogated – a formal document has to be signed between the region and the center that states that the prior agreement is annulled.<sup>209</sup> Moreover, the Kremlin made it clear that it was not interested in the first option, and

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<sup>207</sup> Putin's institutional innovations are enumerated in Chapter 1, and his effort to institutionalize intergovernmental relations and create a "market-preserving" system of federalism will be examined in greater detail in Chapter 6.

<sup>208</sup> A handful of governors criticized Putin's envoys for firing or appointing heads of federal agencies within their regions without first consulting with them. Bashkortostan President Murtaza Rakhimov warned that he would cut off the telephones of all leaders of federal departments and not allow them to work in the republic if they were appointed without his consent. Rakhimov, together with Sverdlovsk governor Rossel and Udmurtiya President Aleksandr Volkov, circumvented Putin's decree on removing the governors' role in appointing the regional head of the All-Russia State Television and Radio (VGTRK) by setting up an alternative television broadcasting company. "Some Governors Increasingly Defiant," *Russian Regional Report*, Vol. 5, No. 39, 23 October 2000.

<sup>209</sup> The documents stipulating the dissolution of the agreement are published in *Rosiiskaya Gazeta*, where federal laws and decrees are promulgated.



avored doing away with all the treaties altogether, many of which directly challenged federal supremacy.<sup>210</sup>

In July 2000, President Putin formed a commission to begin the task of revamping the distribution of authority and responsibilities (e.g. spheres of competency) between Moscow and the regions. The commission was tasked with formulating a package of laws to be submitted to the State Duma in June 2002. Deputy head of the Presidential Administration, Dimitry Kozak, who Putin chose to head the commission, announced that he would give priority to examining the power-sharing treaties between the federal government and the regions. Kozak made it clear that many provisions of the treaties, particularly in the areas of environment, health, regulation of trade and resources, etc. could be addressed in separate agreements between the corresponding regional and federal ministries. Abrogation of the treaties by July 2002, the deadline contained in the 1999 law, was high on the Kremlin's agenda; Putin's "state of the nation" addresses in 2001 and 2002 included an exhortation to regional leaders to comply with federal efforts to dismantle the bilateral agreement system.<sup>211</sup> Putin tasked his seven presidential envoys – the leaders of Russia's newly formed federal districts – to oversee the process

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<sup>210</sup> For instance, the Russian Constitution (Article 11) authorizes the transfer of authority from the federal to regional governments based on bilateral agreements; at the same time, the Constitutional Court ruled that such agreements cannot violate federal legislation. Thus, by submitting legislation contradicting the agreements, the government could in effect nullify various parts of the power-sharing treaties.

<sup>211</sup> In his address in 2002, Putin noted that the agreements cause asymmetry not only between regional governments, but between citizens themselves. He noted that there should be an opportunity for bilateral agreements between the center and regions, but that it was improper to conclude such agreements "behind the backs of other subjects of the federation, and without preliminary discussion and a social consensus." He then went on to stress that any bilateral agreements between Moscow and a particular region governing the division of spheres of competency must be passed by parliament.

of dismantling the bilateral treaty system that had characterized Russian federalism since 1994.

The presidential envoys began their campaign in earnest in May, 2001, and by February 2002 almost two dozen regions had officially given up their agreements.<sup>212</sup> Commenting on the reasons why they acquiesced, some governors went as far as publicly condemning the treaty-signing process and the asymmetrical federal system that it had formed, and urging other governors to follow in their footsteps. For instance, Perm governor Yuri Trutnev, in explaining his decision to become one of the first regional leaders to abrogate a treaty, stated that many articles contained in separate protocols were never realized – in particular personnel decisions, which were supposed to be a joint competency but were de-facto controlled by the center. Trutnev also complained that many parts of the treaty were vague and exceeded constitutional norms, and that there was no provision for sanctions against the federal government in the event of non-compliance.<sup>213</sup>

While some regions more readily acquiesced to the Kremlin, others actively resisted. Several regions were labeled as “problem regions” by the Kremlin due to difficulties in negotiating over the bilateral treaties.<sup>214</sup> For instance, Sverdlovsk governor Rossel categorically refused to sign a document sent by Moscow in February 2002 that

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<sup>212</sup> Mari-El, Astrakhan, Ulyanovsk, Kirov, Chelyabinsk, Omsk, Perm, Magadan, Saratov, Buryatia, Altai, Amur, Kostroma, Nizhegorod, Rostov, Sakhalin, Tver, Yaroslavl and Samara were in the “first wave” of regions reneging their power-sharing treaties.

<sup>213</sup> “Dlya Nashey Oblasti Privilegii net,” *Noviy Kompan'on*, No.24 (177), 17 July 2001, 1.

<sup>214</sup> Indeed, several regions were identified by the Kremlin as “problem regions” due to their particular defiance of the Kremlin’s campaign to phase out the treaties, including Sverdlovsk, Kaliningrad, Bashkortostan, Tatarstan, Moscow, and St. Petersburg according to the head of the main legal directorate of the President, Larissa Brycheva on 19 February 2002. See also Lyudmilla Romanova, “Gubernatoram Ugrozhayut Otstavkoy,” *Nezavisimaya Gazeta*, electronic version accessed March 5, 2002.

would officially abrogate the treaty, instead forwarding his own version of a new treaty to the Kremlin.<sup>215</sup> Later, on 25 July 2002, on the eve of the July 31 deadline, governor Rossel proclaimed that the *oblast* administration still would not reconsider the agreement signed with Moscow.<sup>216</sup> Deputy head of the presidential administration Kozak retorted that according to the 1999 law, as of August 1<sup>st</sup> the center had the right to protest the agreement either in the Sverdlovsk or Ural federal district Prosecutor's office. Rossel reminded him that any sections of the agreement that violated federal legislation were automatically void in any case, but that most of the treaty would still be in force until otherwise changed. Apparently, Rossel was pinning his hopes on both the ambiguous legal situation surrounding the treaties and his ability to lobby parliament when it considered new legislation affecting the treaty areas, rather than attempt to renegotiate with the Kremlin directly. In mid-2002, Kozak's legislative packet envisioned over 300 amendments to existing legislation, and the sheer volume of the legislation gives the governors ample opportunity for defending their interests.

Other governors have attempted to leverage compliance into gaining economic concessions. St Petersburg governor Vladimir Yakovlev reportedly raised the issue of receiving additional funds for his city's 300<sup>th</sup> anniversary celebrations during a meeting with the presidential administration to discuss the power-sharing treaty. Likewise, Kaliningrad has asked for special economic status before giving up the document.<sup>217</sup>

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<sup>215</sup> Alexander Polozov, "Rossel Predlagaet Peresmotret' Svoy Dogovor s Kremlem," *Strana.ru*, accessed February 2, 2002.

<sup>216</sup> "Sverdlovskaya Oblast: Obladministratsiya ne Budet Peresmatrivat' Dogovor s Federal'nyim Tsnetrom o Razgranichenii Polnomochii. [www.regions.ru](http://www.regions.ru) Accessed 25 Jul 2002.

<sup>217</sup> Maria Arzumanova, "Pochemu Dogovornaya Praktika ne Ustraivaet Federal'ny Tsentr?" *Strana.ru*, accessed March 15, 2002.

Irkutsk governor Boris Govorin stated that his region was unwilling to give up the guarantee of its control over 15.5% of Irkutskenergo, the regional electric company, enshrined in the agreement. The company was won by his predecessor in a hard fought legal battle with the federal government in 1993, and apparently the federal government wanted the shares for itself. Finally, the power sharing treaties also had symbolic (ideological) value, as a testimony to the region's – and in many cases, the incumbent executive's – drive for autonomy and success in being recognized on an equal status with the federal center.<sup>218</sup>

In some cases, defiance has paid off. As the center began its harmonization campaign, Tatarstan officials refused to part with their treaty, claiming that it was an integral part of the republic constitution and that a new agreement could not be negotiated without a regional referendum. At the same time, the republic adamantly resisted pressure from Moscow to revise its constitution in full accordance with the federal one, as ordered by the Russian Constitutional Court. In exchange for concessions on the Tatar side, the federal center offered the republic a highly preferential regional development program in summer 2001.<sup>219</sup> Even so, the new Tatar constitution drafted in spring 2002 kept thinly veiled language concerning the republic's sovereign status, its right to offer separate citizenship, and dual language requirements for presidential candidates, and also

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<sup>218</sup> Ibid.

<sup>219</sup> Sergey Mikheev, "Shamiyev Ustupat' ne Sobiraetsya. Poka," politcom.ru, accessed 17 March, 2003. Mikheev notes that the federal program *Social and Economic Development of Tatarstan through 2006* allots the republic over 20 times more funds per capita than for Southern Russia federal district, for instance.

made mention of the bilateral treaty as making up part of the basic law of the region, on the same level as the Russian Constitution.<sup>220</sup>

Likewise, by spring 2002 Bashkortostan's draft constitution – the result of two years of negotiations between Moscow and Ufa – was still ruled by the republic's Supreme Court to contain 33 contradictions with federal legislation, forcing the federal district prosecutor to intervene.<sup>221</sup> Finally, in December 2002, the republic's parliament approved a constitution that contained neither with the term “sovereign” nor the text of the 1994 power-sharing treaty (along with mention of its previous referendum on sovereignty). The republican administration was also forced to both give up its right to appoint mayors and to withdraw its exclusive claim on the region's natural resources. Like the case with Tatarstan, though, Moscow was forced to offer concessions in return for compliance. The republic's president, Murtaza Rahkimov, was given the blessing by the Kremlin to switch the dates for presidential and parliamentary elections in the republic, effectively extending his term by one year.<sup>222</sup> At the end of 2002, the republic still had not abrogated its power-sharing treaty, insisting on renegotiation instead of abrogation.

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<sup>220</sup> At the same time, the republic did remove language asserting that relations with Moscow were subject to international law, and that republican laws take precedence over federal ones. The April 2002 draft constitution identified the republic as a state united (ob'edinennoe) with the Russian Federation based on the RF Constitution, Constitution of Tatarstan and agreement between Moscow and Kazan, and a subject of the Russian Federation. It gave the Tatar Constitution precedence in areas not covered by federal legislation. Vera Postnova, “Kazan' ne Postupilas' Printsipami,” *Kommersant*; electronic version accessed May, 13, 2002.

<sup>221</sup> Gul'chachak Khannanova, “Vtoraya Vlast Pozhalovalas' na Tre'tyu,” *Kommersant*, electronic version accessed April 8, 2002. Part of the problem was confusion surrounding the bilateral agreement, which is included in the republic's constitution. Moscow had yet to decisively claim that the document no longer had any force.

<sup>222</sup> See Sergey Mikheev, “Vy nuzhdennaya Druzhba, Otlozhennaya Voina.” *Polit.com*, accessed March 17, 2003. Mikheev notes that Presidential envoy Sergey Kirienko was involved in the decision.

All in all, the pattern of loyalty and defiance to the Kremlin's efforts to harmonize their relations with the center has been a significant measure of its political leverage over various regions, in addition to a particular region's commitment to the formal component of autonomy, whether due to concrete privileges and property rights or the political value of the treaty for the regional government. It is interesting to note that while the presidential envoys have been the driving force behind the campaign to pressure regional governments into abrogating the treaties, they have had mixed success within their own districts. Thus, while Kirienko was able to pressure most regions in his district to abrogate their treaties, including Nizhny Novgorod, Perm, Samara and Orenburg, others, such as Tatarstan, Bashkortostan and Udmurtia, remained in non-compliance past the July 2002 deadline. In the Siberian federal district Leonid Drachevsky has had success with Altai, Buryatia and Omsk, but not with Irkutsk and Krasnoyarsk at the time. Likewise, of the two regions in the Urals federal district that signed agreements with the center, presidential envoy Petr Latyshev has forced Cheliabinsk into giving up its agreement, but was not able to convince neighboring Sverdlovsk as of August 2002. In the Far East, Konstantin Pulikovskii was able to convince Magadan and Sakhalin, but not Khabarovsk and Sakha-Yakutia until after the deadline, in fall 2003. Moreover, the resigning of an amended power-sharing treaty with Sakha-Yakutia in October 2002 is evidence that Moscow is prepared to make exceptions in its campaign to do away with the whole practice.<sup>223</sup>

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<sup>223</sup> The amended treaty was signed in October 2002. Treaty accessed in Rossiiskaya Gazeta archives, [www.rg.ru](http://www.rg.ru). The Kremlin resigned the treaty after it had successfully engineered the removal of the incumbent leader, Nikolyaev from office, replacing him with a more "loyal" candidate.

## **Putin's First Term: Revolution or Evolution?**

In terms of federal strategy, the starkest contrast has been evidenced between the Yeltsin and Putin presidencies. Putin's most important achievement has been to move the main venue of intergovernmental decision-making (e.g. dispute resolution) on jurisdictional and distributional issues from the realm of unilateral actions (phase 1) and bilateral bargaining (phase 2) to collective-decision making institutions such as parliament, as well as a reformed court system.<sup>224</sup> Collective decision-making institutions should produce more transparent and fair rules that will lay the foundation for greater consensus among elites on the legitimacy of Russia's federal system.<sup>225</sup> To the extent that the center is able to maintain a united front and sanction assertiveness from below, regional elites will be increasingly forced to channel their rent-seeking activity into more traditional – and less politically destabilizing – tactics for asserting particularistic interests in democratic federations, such as log-rolling, coalition-building, committee assignments etc.

Yet, there are two major aspects of continuity to be found in the federal center's behavior, in particular in its use of informal vs. formal rules in dealing with the periphery. First, the Kremlin has continued to actively manipulate the internal political

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<sup>224</sup> One of Putin's major domestic accomplishments in his first term has been judicial reform, a large part of which is aimed at reestablishing the court system hierarchy throughout the country, and standardizing procedures. Kozak was also in charge of preparing legislation for this reform effort.

<sup>225</sup> Even if distributional rules are asymmetrical (e.g., favoring one region over others), the decision-making process is paramount to ensuring consensus. Federal legislative venues such as parliament are the only ones which collectively include representatives from all regions in the decision-making process. For example, Stepan, notes that the decision to grant Spain's autonomous regions special status was made collectively at the national level (parliament) rather than as a special deal between executives. The result was greater intergovernmental stability and consensus during the transition, as opposed to the Russian case. See Stepan, 2000.

situation in various regions, especially during election campaigns, as a means of dislodging recalcitrant regional leaders. While the Kremlin had at best lackluster success during the 1996-1997 regional election cycle, by 2000-2001 it had further refined its tactics and expanded its arsenal of actors. Compared to his predecessor, Putin has made much greater use of state resources “on the ground” in a particular region, such as the federal district apparatus, prosecutors, court system, and the Federal Security Service (FSB). Regime changes in Yakutia, Ingushetia and Perm are some of several examples where direct intervention via state agencies and institutions played a major role.<sup>226</sup>

Interestingly, the use of these "sticks" in a region has been accompanied with "carrots" as well. This has been demonstrated most vividly by the deals made with regional leaders whom the Kremlin has convinced to voluntarily leave office, which have included federal-level appointments such as high-level positions in the Federation Council (former Sakha governor Nikolayev) or in the federal government (former Maritime province governor Nazdratenko) or even in the Cabinet (former St Petersburg governor Yakovlev). Thus it appears that personal inter-elite negotiating is still an essential element of the Kremlin's leverage over the regions, as during the Yeltsin era.

While Putin is in a superior bargaining position compared to his predecessor, he has

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<sup>226</sup> Vladimir Gelman, “Evolving Trends: Democratic Gains Reversed in Regional Elections from Moscow to Sakha.” *Russian Regional Report*. Vol. 7, No. 5, 6 February 2002. It was widely recognized that the federal center undertook a concerted (though unofficial) campaign to unseat the longtime incumbent, President M. Nikolayev, via manipulation of the court system and the federal and local prosecutor offices. Nikolaev finally buckled under pressure from the Kremlin and withdrew from the race. The Kremlin-backed candidate, V. Shtyrov, the director of AlRosa, easily won the election, and several months later the republic agreed to amendments to its treaty with the federal center with concessions to Moscow regarding the diamond company and the region’s natural resources. In Ingushetia, the candidate backed by the local regime, Khamazad Gutseriev, was forced to withdraw on a technicality after interference by presidential envoy Victor Kazantsev. Following Gutseriev's disqualification, Federal Security Service General Murat Zyazikov, a deputy to Kazantsev, was elected in a second round victory. In Perm, presidential envoy Sergei Kirienko successfully mobilized the region’s resources against the incumbent Igumnov.



nonetheless eschewed the use of formal procedures for removing governors of regions in violation of federal legislation from office enshrined in legislation passed in the beginning of his term. This could, of course, indicate that it is particular political or personal agendas rather than objective constitutional violations that motivate the Kremlin's decision to pressure certain regional executives to step down.<sup>227</sup>

Secondly, various observers have noted that the approach of the 2003-2004 federal election cycle caused the Kremlin to temper its centralization drive somewhat. This has been particularly demonstrated by the Kremlin's backtracking on legislative initiatives to limit governors' monopoly over political resources in their regions, such as restrictions on term limits and instilling party-list voting in regional legislative elections.<sup>228</sup> Indeed, an amendment passed in January 2001 with the active support of the pro-Kremlin Unity party gave 69 of Russia's 89 regional leaders the opportunity to run for a third term, and 17 – mostly republican leaders – for even a fourth.<sup>229</sup> Additionally,

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<sup>227</sup> For instance, clan based rivalry might have motivated the Kremlin's offensive against governors associated with Yeltsin's "Family," such as Spiridonov in Komi and Nikolayev in Yakutia. Also, Putin had never been fond of St Petersburg governor Yakovlev after they ended up on different sides of the mayoral election campaign in 1996.

<sup>228</sup> See especially Gelman, "Evolving Trends..." Two of Putin's major legislative initiatives designed to rein in regional leaders have included a law limiting governors to two terms (incumbent advantage – access to administrative resources – is often a prevailing factor in regional elections) and mandating that regional legislatures allot half their seats to party list candidates (to increase penetration of federal parties in the periphery). Ultimately, the former law was amended to allow a third and in some cases fourth term for governors in certain cases, while the Kremlin has put the latter on the back burner. The Kremlin's about-face on the gubernatorial term limit law was widely regarded to be a concession to regional heavyweights such as Moscow Mayor Yuri Luzhkov and Tatarstan President Mintimer Shamiyev in exchange for their electoral support. Other executives not in favor with the Kremlin were pressured not to run (Nikolyaev in Yakutia, Aushev in Ingushetia), or were blocked on technicalities (e.g. St Petersburg Governor Yakovlev).

<sup>229</sup> Federal legislation dictates that governors are allowed only two terms; the amendment, however, moved up the date that the legislation became effective to just before the second round of gubernatorial elections in 2000-1, in effect discounting their first term. Leaders already in their second term, especially republican presidents who had achieved early elections (e.g. 1991-1993) were allowed to "start from scratch," and run for two more terms if regional legislation allows. Dimitry Kamyshev, "Tatarskii Pretsident," *Kommersant*, January 30, 2001. Electronic Version.

specific concessions have been made to certain regional heavyweights in exchange for their willingness (and demonstrated ability) to "deliver the vote" during parliamentary and presidential elections.<sup>230</sup> This pattern is similar to the one evidenced during the 1995-1996 election cycle, when the Kremlin also made major concessions to assertive regional elite in the power-sharing treaties and allowance of early elections. As Gel'man notes, Putin, like his predecessor, has concluded an "informal contract" with regional elites, allowing them to further consolidate their authority in their jurisdictions in exchange for electoral support.<sup>231</sup>

Thus, while Putin has made significant progress in building the formal institutional framework for a rule-based, democratic federal system, the Kremlin still has preferred to play by the informal rules of the game when the stakes are higher, as demonstrated by its interference in regional elections and strategic accommodation of regional leaders ahead of the federal election cycle. These elements of continuity are important when considering regional elites' rational expectations. The defensive form of assertive regionalism under Putin, expressed as defiance of federal efforts to harmonize intergovernmental relations, is still the product of the same cost-benefit calculations as the offensive form of regionalism that characterized the 1990s. Both are based primarily

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<sup>230</sup> Sergey Mikheev, "Vynuzhdennaya Druzhba, Otlozhennaya Voina," Politru.com accessed March 17, 2003. Examples of the latter include turning a blind eye both to Bashkortostan President Rakhimov's decision to effectively extend his term for a year by switching regional-level presidential and parliamentary election dates in the republic, and to Tatarstan's recent State Council election, which violated federal legislation, as well as grudging support for Sverdlovsk governor Eduard Rossel's re-election campaign by the Kremlin's party of power, United Russia.

<sup>231</sup> Gel'man, "Evolving Trends..." In essence, a tactical "cease-fire" with defiant regions. Treisman, *After the Deluge*, 1999, also points to an informal political exchange as underlying intergovernmental relations in the Yeltsin era: central accommodation (in this case, increased transfers) in exchange for regional support during the federal election cycle. The additional funds translated into political dividends for the governors as well, who were able to pay state salaries on time and meet other fiscal obligations.

on informal rules, mainly the bargaining chips available to the region to influence the balance of power at the federal level, and thus the center's political will to either use the formal sticks it has available or to "bend" the rules in the region's favor. Table 3.3 below shows a partial listing of assertive actions by Russia's wealthy regions across the three phases outlined in this chapter.

Table 3.3: Assertive Regionalism among Heavily Industrialized Regions, 1990-2002

<b>Phase 1, 90-93: Expanding Autonomy</b>	
<i>Declarations of “Republic” Status (1990-1993)</i>	(1990) <i>Republics</i> of Bashkortostan, Komi, Sakha-Yakutia, Tatarstan, Udmurtiya (1993) <i>Oblasts</i> : Sverdlovsk, Vologda, several others begin preparations
<i>Early Elections (1991)</i>	<i>Republics</i> of Tatarstan and Sakha-Yakutia; Cities of St. Petersburg and Moscow, other republics
<i>Referenda on a region’s status (1992-1994)</i>	<i>Republics</i> of Bashkortostan and Tatarstan; <i>Oblasts</i> : Irkutsk, Sverdlovsk, and Vologda
<i>Tax Rebellion, 1992-1993</i>	<i>Republics</i> of Bashkortostan, Komi, Sakha-Yakutia, Tatarstan and others; <i>Oblasts</i> : Chelyabinsk, Irkutsk, Khabarovsk, Krasnoyarsk, Samara, Sverdlovsk, Volgograd, etc.
<b>Phase 2, 94-98: Formalizing Gains</b>	
<i>Early Elections, Oblasts (before 12/95)</i>	Sverdlovsk and Irkutsk
<i>Early Power-Sharing Treaty (before June 1996 presidential elections)</i>	(1994-1994) <i>Republics</i> of Bashkortostan, Sakha-Yakutia, Tatarstan and Udmurtiya (1996) <i>Republic</i> of Komi; <i>Oblasts</i> : Irkutsk, Khabarovsk, Nizhny Novgorod, Omsk, Orenburg, Perm, St Petersburg, Sverdlovsk, and others
<i>“Economic Revolt”, 1996-1998</i>	<i>Republic</i> of Tatarstan; <i>Oblasts</i> : Irkutsk, Khabarovsk, Krasnoyarsk, Maritime, Omsk, St. Petersburg, Sverdlovsk, Tula and others
<b>Phase 3, 1999-2002: Defending Gains</b>	
<i>“All Russia” party leadership council, 1999 (regionalist party building)</i>	<i>Republics</i> of Bashkortostan and Tatarstan; <i>Oblasts</i> : Irkutsk, Khabarovsk, and St Petersburg
<i>Treaty Abrogation: “miss” July 2002 deadline*</i>	<i>Republics</i> of Bashkortostan, Sakha-Yakutia, Tatarstan, Udmurtiya; <i>Oblasts</i> : Irkutsk, Krasnoyarsk, Khabarovsk, Murmansk and Sverdlovsk
<i>Labeled as “Problem Regions” by the Presidential Administration**</i>	<i>Republics</i> : Tatarstan and Bashkortostan <i>Oblasts</i> : cities of Moscow and St Petersburg, Sverdlovsk
Leaders (regions assertive across all three phases in at least one category):	<i>Republics</i> : <u>Tatarstan</u> (all relevant categories), plus Bashkortostan, Sakha-Yakutia & Udmurtiya; <i>Oblasts</i> : <u>Sverdlovsk</u> (all but one) plus Irkutsk, Khabarovsk, Krasnoyarsk & St. Petersburg

\*Based on official notice of abrogation in *Rossiiskaya Gazeta*. Sakha and Khabarovsk did comply in late 2002, after the July 2002 deadline; Sakha renegotiated, while Khabarovsk rescinded the treaty. Other instances of abrogation occurring after 2002 are not included in this table: the assertiveness index covers the period from 1990-2002.

\*\* As of February 2002 (see fn 214)

## CONCLUSION

While assertive regionalism took different forms across the three phases of intergovernmental relations from 1990-2002, the overall nature of the bargaining game has remained the same. Whereas in the first two phases, assertive regions took the offensive and attempted to use declarations, ultimatums, referenda, “tax revolts” etc. to coerce the center into accommodations over jurisdictional and/or distributional rules, in the third phase the regions were put on the defensive. After an abortive collective effort by both ethnic and non-ethnic regions in the 1999 parliamentary elections to change the balance of power at the federal level in their favor, assertiveness reverted back to its most typical form in the 1990s – with individual regions rather than coalitions as the main actors– although now it has taken on a distinctly defensive form. Assertive regions have tried to “wait out” the center’s siege by resisting the implementation of federal legislation on the harmonization of the federal rules. Defiant executives do have some rational expectations of success: in all three phases, Moscow has evidenced a willingness to negotiate. Putin, in particular, has avoided direct confrontations with defiant regions, preferring to work behind the scenes and through various federal agencies in the periphery.

Given the federal center’s propensity for informal rules and selective accommodation throughout the transition period, the various forms of assertive regionalism can be viewed as part of a continuous strategic effort to secure regional autonomy, with the rational expectation that sufficient resolve and bargaining power will lead to concessions. Of course, the nature of the accommodations has changed

dramatically, from Yeltsin's "take all you can handle" in 1990 to Putin's grudging tactical retreats in selected areas prior to the 2003-2004 election cycle. While the entire period from 1990-2002 was characterized by the predominance of intergovernmental bargaining over the federal rules, some regions consistently pursued assertive strategies. The unilateral actions that characterized the first phase were important bargaining chips, in terms of credibility of threats and reputation of regional executives, for negotiations with Moscow in the second phase. Defense of the political autonomy formally devolved to the regions in the second phase then served as bases of political mobilization and individual instances of defying Moscow in the third phase.

This period demonstrated two uniform patterns in regional behavior, with certain regions, such as the republics of Tatarstan and Bashkortostan, and Sverdlovsk *oblast*, consistently assertive across all three IGR phases. At the same time, other highly industrialized regions, such as Samara, Perm, Nizhny Novgorod and Tomsk, more often displayed "loyalty" to the federal center. This wide range of variation in regional behavior will be examined statistically in Chapter 4.

## **Chapter 4: Testing the Theory**

This chapter provides empirical evidence that national-level businesses have helped to structure more cooperative patterns of center-periphery relations throughout Russia's democratic transition. The top echelon of individual enterprises and vertically-integrated energy companies has served as a “tie that binds” federal and regional elites’ political interests by acting as a shared resource, explaining unexpected restraint among wealthy regions in the context of under-institutionalization of the federal system and weak national party penetration in the periphery.

The first section of the chapter identifies the “national-level” subset of Russian businesses based on two major criteria – size and corporate structure – that influence the degree to which various types of alliances between big businesses and political elites fragment or integrate the federal state. The institutional context that has amplified the political role of big business in Russia’s federal system is then overviewed. The next section constructs the dependent variable, the regional assertiveness index, based on the observations outlined in the previous chapter, and then lists the control variables found in the comparative literature. Several versions of multivariate regression analysis are then presented. Finally, the theoretical implications of the findings are discussed, setting the stage for the qualitative analysis in the following chapter.

## IDENTIFYING NATIONAL-LEVEL BUSINESSES

### Criterion #1: Size

The main criterion for national-level business is size, which is a measure of an enterprise's strategic importance in the national economy, as well its influence in a given region.<sup>232</sup> While many large businesses have the resources to forge symbiotic, informal ties with regional administrations, only a handful of strategically important business actors have the clout to also maintain steady channels of influence to key policymakers at the federal level. It is this “vertical,” or intergovernmental, aspect of business alliances with federal and regional levels of government that is important in terms of their ability to integrate rather than fragment the federal state. In addition to its influence over a particular level of government, the size of an enterprise also determines its level of dependence: the larger the enterprise and the more important role it plays in the national economy and federal budget, the more apt it is to remain under the scrutiny of federal politicians, which makes it less able to “hide” behind the patronage of regional administrations.

The measure used for size is the volume of sales (output), indicative of an enterprise's financial, political and fiscal influence. As evidenced in Table 4.1, Russia's largest enterprises can be divided into two groups, with the top 20 enterprises demarcating a first echelon, or the tip of the pyramid. Stability in the rankings across

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<sup>232</sup> For instance, Pappe makes a distinction between large enterprises in general and those which are strategically important at the national level; the latter are constantly under the patronage as well as the oversight of the federal government. See Yakov Pappe, “Treugol'nik Sobstvennikov v Regiona'Inoy Promyshlennosti (The Triangle of Stakeholders in Regional Industry),” in Klimanov and Zubarevich, 2000, 109-121.



time demonstrates that a relatively distinct cohort of business actors occupy this first echelon; other enterprises have broken into the top rank for brief intervals (e.g. one or two years maximum), and then in most cases only to 19<sup>th</sup> or 20<sup>th</sup> place.

Table 4.1: First and Second Echelon Enterprises, 1995-2001<sup>233</sup>

Name	Sector	95	96	97	98	99	00	01	Avg. Rank	Avg. Output \$, million
<b>First echelon companies</b>										
1. Gazprom	Natural Gas	2	2	2	2	1	1	1	2	20,128
2. UES	Power	1	1	1	1	3	3	2	2	17,362
3. Lukoil	Oil/gas	3	3	3	3	2	2	3	3	11,512
4. YUKOS	Oil/gas	6	5	6	9	7	4	4	6	6,776
5. Surgutneftegaz	Oil/gas	7	6	5	6	4	5	5	6	5,336
6. Norilsk Nickel	Non-Ferrous	9	11	9	8	5	6	9	8	4,080
7. Avtovaz	Auto	8	7	7	7	8	12	8	8	3,132
8. Tatneft	Oil/gas	12	8	11	13	10	8	11	10	3,713
9. Sibneft	Oil/gas	---	9	8	10	12	11	10	10	2,906
10. Tyumen Oil	Oil/gas	10	17	17	11	11	7	6	11	3,298
11. Sidanko	Oil/gas	5	4	4	5	20	22	16	11	3,090
12. Rosneft	Oil/gas	11	12	12	16	9	9	13	12	3,144
13. Severstal	Metallurgy	14	15	13	12	14	13	15	14	2,290
14. Slavneft	Oil/gas	---	19	14	15	15	10	12	14	2,264
15. Bashneftkhim	Oil/gas	---	10	10	4*	6*	17	26	15	2,378
16. Magnitogorsk	Metallurgy	15	14	19	18	16	15	17	16	2,067
17. AlRosa	Diamonds	19	21	20	14	13	14	14	16	1,725
18. Novolipetsk	Metallurgy	13	16	18	19	17	16	21	17	1,879
19. Bashneft*	Oil/gas	25	13	15	---	---	18	18	18	1,959
20. GAZ	Auto	17	20	16	17	18	20	27	19	1,453
<b>Reference: Top five in second echelon</b>										
21. Orenburg Oil	Oil/Gas	20	26	21	20	19	23	---	22	883
22. Nizhny Tagil	Metallurgy	18	22	22	30	25	27	---	24	1,076
23. W Sib. Metal	Metallurgy	21	24	31	26	22	29	---	25	833
24. Krasnoyarsk Aluminum	Non-Ferrous	23	29	24	25	21	28	---	25	737
25. Nizhekamsk	Oil/gas	31	28	23	24	23	25	34	27	777

<sup>233</sup> Source: *Expert* Top 200 Russian Enterprises, 1996-2002 issues. Average output for 1996 and 2001 (some oil companies did not report this data in 1995). \*Bashneftkhim and Bashneft were consolidated under Bash Fuel in 1998 and 1999.

<b>Reference: Mergers, Newcomers in Top 20</b>									
Eastern Oil	Oil/Gas	16	18	---	---	---	---	---	Acquired by Yukos (#5)
Rusal	Non-Ferrous	---	---	---	---	---	---	7	Inc. Kras. Al. (#24)
EvrazHolding	Metallurgy	---	---	---	---	---	---	19	Inc. Nizhny Tagil (#22)

Altogether, the top twenty enterprises represent the “commanding heights” of Russia’s national industry. In addition to domestic production, all these enterprises are heavily oriented toward international markets, making them key sources of hard currency receipts, which increases their dependency on the federal level of government.<sup>234</sup> In addition to the highly lucrative oil and gas sector, the list includes the “big three” of Russia’s steel industry – Severstal, Magnitogorsk and Novolipetsk – Russia’s top auto producers, VAZ and GAZ, and the non-ferrous giant Norilsk Nickel.

## **Criterion #2: Structure**

The second criterion, which applies specifically to the oil and gas sector, is corporate structure, or the level of vertical integration. While metals and machine-building enterprises have one primary production (e.g. manufacturing) asset and headquarters concentrated in the same town or district, oil holdings have multiple assets across the production chain (e.g. individual extraction units, refineries, petrochemical plants, etc.), which are dispersed throughout multiple districts or regions. Unlike metals

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<sup>234</sup> For the period of observations, 1990-2002, the largest Russian businesses were all primarily export-oriented, save RAO UES. The energy VICs are especially dependent on the federal government’s control over gas and oil export pipelines, as well as federal-level taxation of resource extraction and exports (e.g. via State Customs Committee). In addition, many export-oriented or import-substitution sectors, such as metals and automotive companies, rely on national policymakers for defense of their interests abroad and for export quotas or favorable import tariffs.

and machine-building giants, constituent enterprises of oil holdings by themselves are generally not large enough to be strategically important in the national economy, and thus have to rely on integration into a larger corporate structure for steady channels of influence at the federal level.<sup>235</sup>

Under the Soviet Union's system of economic "departmentalism", or administrative regionalism in industry, vertical ties between an individual enterprise and the relevant sectoral ministry were much more important for successful business operations than "horizontal" ties to enterprises in neighboring regions, as is the case in a market economy.<sup>236</sup> During the phase of spontaneous privatization as the Soviet governmental ministries crumbled in the late eighties and early 1990s, groupings of federal and regional bureaucrats and politicians fought to gain control over privatization of the fragmented oil industry. State monopolies such as Gazprom (natural gas) and RAO UES (electric power) are the most successful examples of reconstructed economic hierarchies, and together with Moscow-based oil holdings and financial-industrial groups they have served the purpose of economic reintegration (e.g. consolidation of federal-level control over the country's key assets).

Thus for individual oil and gas assets, corporate structure is significant, since smaller, geographically dispersed assets need to be organized in order to act collectively. The key to differentiating between national- and regional-level oil companies is the

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<sup>235</sup> Basically, an economy of scale effect in terms of lobbying power.

<sup>236</sup> See Vladimir Gel'man, Sergei Ryzhenkov and Michael Brie, *Making and Breaking Democratic Transitions: The Comparative Politics of Russia's Regions* (Lanham, Maryland: Rowman and Littlefield: 2003), 44-50, and Sergey Pavlenko, "Administrative Regionalism: Stages, Actors, Legitimization and Prospects," in Klaus Segbers/Stephan De Spiegeleire, eds., *Post Soviet Puzzles: Mapping the Political Economy of the Former Soviet Union* (Baden-Baden: Nomos Verlagsgesellschaft, 1995).

degree of vertical integration across regions. Table 4.2 ranks the first-echelon oil and gas companies according to the degree of their vertical integration.

Table 4.2: Structure of First-echelon Oil and Gas Enterprises, 1995 <sup>237</sup>

<i>Company</i>	<i>Level of Vertical Integration</i>
Gazprom	Very High
Lukoil	High
Surgutneftegaz	High
Sibneft	High
YUKOS	Medium
Sidanko	Medium
Rosneft	Medium
Slavneft	Medium
Tyumen Oil	Low/Medium
Tatneft	None
Bashneft	None

In three cases, vertical integration on the national level has been absent: Tatneft (#8) Bashneft (#19)/Bashneftkhim (#15). Indeed, the republics of both Tatarstan and Bashkortostan managed to stave off the integration of oil assets on their territories into Moscow-based holdings during the early phase of privatization, instead setting up regionally-based companies. At the same time, other ethnic republics, such as Udmurtia, as well as the wider set of oil-producing *oblasts*, were less successful in this regard, and saw a good portion of their oil industry absorbed into national-level businesses. Among the integrated oil majors, Tyumen Oil has had a more decentralized and regionally-based corporate structure, although it was acquired by Alfa Group, which is headquartered in

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<sup>237</sup> Source: David Lane and Iksander Seifulmulukov, "Structure and Ownership [of the Post-Soviet Russian Oil Industry]," in David Lane, ed., *The Political Economy of Russian Oil* (Lanham: Rowman and Littlefield Publishers, 1999), 21.

Moscow. Due to their “flat”, e.g. regional structure, Bashneft and Tatneft will be considered as regional-level businesses, while Tyumen Oil is tested both ways, as both a national- and regional-level enterprise.

Again, this second criteria does not apply to the single-actor machine and metal giants, since they do not face the organizational/collective action dilemmas that the various production and refining units do in oil companies, which need to be united under one roof to act as a single entity. If the “roof” was built by national-level bankers and bureaucrats, and vertically integrated across regions, then these assets would be beholden to federal level actors, while those organized by regional elites, with nationally decentralized structures, would be more beholden to that region for their livelihood and less likely to act independently of its leadership.

### **Political-Institutional Context**

The political and economic environment in Russia during the first dozen years of the transition has magnified the influence of big business on the federal, and especially regional, levels of government. Due to the underdevelopment of market and legal institutions, the post-Soviet political economy has remained highly politicized, forcing businesses to seek stable, mutually beneficial alliances with political elites in order to compete – and survive – on regional or national markets.<sup>238</sup> In particular, national-level business actors are primarily dependent on alliances with federal officials for competition

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<sup>238</sup> Some of the major problems are weak contract enforcement, unstable property rights and inefficient (easily manipulated) bankruptcy legislation, while the judicial branch has been semi-autonomous at best. An overview of the main characteristics of the rent-seeking nature of the Post-Soviet Russian economy can be found in the introduction to Peter Rutland, *Business and the State in Contemporary Russia* (Boulder, Colorado: Westview Press, 2001).

with other rivals on national and international markets, and their aversion to regional (e.g. sub-national) autarky and protectionism – a central ingredient of assertive regionalism in the Russian case – makes them natural allies of the federal center. Due to their political dependence on federal officials and preference for a unified national market space, they are more likely to use their political resources to counter regional assertiveness and mediate intergovernmental disputes in order to ensure a stable operating environment.<sup>239</sup>

While business is apt to seek political patronage due to the politicization of market institutions, the reverse is also true: the inefficiency or weakness of fiscal and political institutions has made politicians more reliant on business for mobilizing resources. Throughout the 1990s, the Russian fiscal system suffered from a cash crunch, due to the inefficiency of tax collection and proliferation of monetary surrogates and barter.<sup>240</sup> For federal level officials, close relations with national-level businesses, especially those with access to hard currency (e.g. export receipts), have been vital for mobilizing financial resources and managing the economy.<sup>241</sup>

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<sup>239</sup> As Polishchuk argues, business actors operating on the national market such as Moscow-based financial industrial groups are interested in national market cohesiveness, including the free movement of labor and capital, and consistent defense of contracts and property rights across various regions. Although they can achieve this via informal ties with various regional officials, ultimately the federal government is the best defense of their national market interests. A single set of rules (and a single enforcer) is more efficient than 89 sets of rules and enforcers (number of Russian regions); a unified national legal space is conducive for economies of scale. See L. Polishchuk “The Russian Model of Negotiated Federalism: a Political and Economic Analysis” in Klimanov, V. and Zubarevich, N, eds., *The Regional Dimension of Politics and Economics* (Moscow, St. Petersburg: Studia Politica, 2000).

<sup>240</sup> See, for instance, Schliefer and Treisman, 2000.

<sup>241</sup> For instance, Gazprom was considered a quasi-fiscal actor due to its fiscal role, such as extending loans to the budget for wage and pension payments and subsidizing inputs (along with UES) across the country. Russia has a “top-heavy” fiscal system, where a narrow group of large companies account for the lion’s share of proceeds. Thus, the government has always leaned on the largest tax payers, such as energy companies – which have steady access to hard currency – rather than raising personal income tax (which would only exacerbate tax evasion).

Furthermore, on the sub-federal level, the fiscal federal system has greatly restricted regional governments' formal authority to raise additional sources of revenue, which was exacerbated by the devolution of social and infrastructure expenditures at the beginning of the transition. Since 2000 an economic recovery has taken place, gradually easing the cash crunch. However, it has also been accompanied by fiscal centralization, with the federal government claiming a larger share of the total pie.<sup>242</sup> Thus, federal encroachment has continued to limit the financial resources available to regional governments, making them not only internally reliant on various informal (extra-budgetary) arrangements, but also highly dependent on external sources of capital.<sup>243</sup>

Turning toward political institutions, the electoral rules and voter behavior undergirding Russia's party system have limited its effectiveness as a vertically-integrating mechanism in Russia's federal system.<sup>244</sup> Meanwhile, regional officials have actively resisted the penetration of national-level parties, making direct alliances between regional executives and business actors virtually indispensable around election time.<sup>245</sup> While Putin's personal popularity and base of support in the security and "law and order" ministries have afforded the national government a much higher degree of autonomy from business, the reverse trend has taken place at the regional level. Political recentralization has deprived regional governments of formal regulatory weapons (and

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<sup>242</sup> *Country Report: Russia* (Paris: OECD, 2000 and 2003)

<sup>243</sup> See for instance, Yuliya Latynina, "Byudzhetny Feodalism," *Expert*, No.1, 12 January 1998, 15-18.

<sup>244</sup> Russia's political party system was under-institutionalized and had little penetration in the periphery during the 1990-2002 period. On the underinstitutionalization of Russia's party system, see especially Robert Moser, "Electoral Systems and the Number of Parties in Post-Communist States," *World Politics* 51 (April 1999): 359-384. On their vertically integrating role, see Ordeshook and Shevtsova, 1997.

<sup>245</sup> Stoner-Weiss, 2001.



hence political leverage) to curb the expansion national-level business actors into the periphery.

Finally, federal systems in and of themselves magnify the influence of big business by offering multiple venues (e.g. access points to government) for actors to pursue their strategic interests. In the triangle of the federal government, sub-national governments and business, the latter is the most mobile, both horizontally, vis-à-vis sub-national governments (e.g. ability to change regional jurisdictions), and, especially, vertically – playing off one level of government against the other to further its own interests. Indeed, business has been named as one of the main culprits for the fragmented social and regulatory policy space in developed democratic federal systems such as the US.<sup>246</sup>

However, the dissertation's thesis implies that in the Russian case, the influence of big business actors has extended beyond the economic and social policy sphere to the nature of political interaction between the center and regions. In line with the bargaining model of federalism, influential non-state actors can be a valuable financial and political resource (or constraint) for one or another level of government.<sup>247</sup> The relative politicization of market institutions and underdevelopment of vertically-integrating

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<sup>246</sup> Robertson and Judd maintain that the multiple veto points and opportunities for goal displacement in the US federal system undermine national policy coherence. The authors' most scathing critique of federalism focuses on the unfettered power of business interests vis-a-vis subnational governments. The ability of capital to "vote with its feet" and use alternate regional or national arenas to advance its interests leaves investment-minded state governments especially vulnerable to particularistic interests. Robertson and Judd argue that the US federal system and ensuing dominance of business vis-a-vis labor has been a principle obstacle to earlier movements to establish a comprehensive welfare system. Robertson and Judd, 1989.

<sup>247</sup> The bargaining model of Russian federalism lasted into Putin's first term as well (up until the 2003-2004 election cycle). See Chapter 3.

institutions, such as national party systems and fiscal federal arrangements, have exaggerated the political role of big business actors in Russia's federal system.

A high degree of mutual interdependence between state and business officials – in particular at the regional level – has been a common thread uniting the index period, 1990-2002. The presence of business actors beholden to the federal government in a region increases the Kremlin's political leverage in the federal bargaining game, to the extent that they force regional elites to “share” control over key assets within their jurisdictions with national elites. At the same time, national-level businesses are also able to co-opt otherwise assertive regional elites by offering various “carrots,” including electoral support and access to outside investment resources. Although regional leaders, *ceteris paribus*, would prefer to have maximum formal autonomy and the largest fiscal distributional gains (and not share them with federal-level actors, e.g. a “winner take all” strategy), such arrangements do provide material and political benefits that can substitute for gains achieved by more assertive – and risky – autonomy-seeking strategies.<sup>248</sup> Finally, big business itself benefits from patterns of exchange and reciprocity giving it influence in executive and legislative decision-making bodies.<sup>249</sup>

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<sup>248</sup> See chapter 5 for specific examples of these “carrots.”

<sup>249</sup> Patterns of exchange include giving business representatives executive posts in the regional (and federal) administration and relevant committee assignments in the legislature (e.g. taxation and economic policy) in exchange for electoral support and financing of public projects, as well as the appointment of regional executives to the boards of corporations and related banks.

## CONSTRUCTING THE MODEL

### Independent Variable

Having identified a stable cohort of “national-level” businesses across time, two methods of constructing the independent variable are suggested: a region’s weight in the national-level political economy or, conversely, the relative weight of national-level business actors in a region’s political economy.

The first variation gauges incentives for national-level actors to “manage” the political situation in a given region. The higher the concentration of nationally strategic assets in a given region, the greater the incentives for national-level businesses, and their patrons, to counter assertive regionalism in order to prevent these assets (or their earnings) from being taken over by regional elites.<sup>250</sup> The second variation measures the influence of national-level holdings in a regional economy. The larger the relative weight of national-level business actors, the greater their ability to influence regional strategic behavior via the “carrots” and “sticks” discussed earlier. Both variations of the independent variable are expected to be negatively correlated with regional assertiveness.

Each variation of the independent variable can be further broken down by sector. Controlling for sectoral differences is important: if it is primarily sector (broadly defined as oil & gas or machine & metals) rather than size and vertical integration that has a greater effect of regional political behavior, then the oil & gas and machine & metals variables should have different signs, or only one should be significant. In the regression

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<sup>250</sup> For instance, autonomy projects in some of the most assertive regions, such as Sverdlovsk and Tatarstan, have included state-led redistribution of profits from the mineral sector toward industry and agriculture.

analysis, each variation of the independent variable will be tested in its aggregate form and then disaggregated by sector, as indicated in table 4.3.

Table 4.3: Operationalization of the Independent Variable

<b>1. National Ratio (<i>NatRat</i>)</b>	<i>Incentives</i> for national-level business actors to influence regional politics, or their “stake” in a region
<b>a. Aggregated</b>	Ratio of the output of national-level businesses in a region to total national-level business output in the country (average for time period, expressed as percent)
<b>b. Disaggregated</b>	
Fuel	---oil and gas enterprises only
Machines/Metals (M/M)	---metallurgy and auto sectors only
<b>2. Regional Ratio (<i>RegRat</i>)</b>	Relative <i>influence</i> of national-level businesses in a regional economy
<b>a. Aggregated</b>	Ratio of the output of national-level businesses in a region to total industrial output in the region (average for time period, expressed as percent)
<b>b. Disaggregated</b>	
Fuel	---for oil and gas enterprises only
Machines/Metals (M/M)	---metallurgy and auto sectors only

National-level businesses include all the top 20 enterprises (first echelon) listed in Table 4.1, with the exception of the oil companies listed in Table 4.2 that were not vertically integrated on the national level during the index period.

### **Dependent Variable: Regional Assertiveness Index**

Table 4.4 provides a detailed breakdown of the assertiveness index. While the forms of assertive regionalism have changed across time as the federal center has strengthened (which has structured a shift from “offensive” to “defensive” assertion under Presidents Yeltsin and Putin, respectively), the substance has remained the same:

securing the dominant elite group's control over political and financial resources within the region. Moreover, the dichotomous pattern among the wealthy regions has remained consistent.

The index includes three areas of regional assertiveness: jurisdictional, distributional and regionalist political mobilization. Jurisdictional issues deal with the formal aspect of autonomy in terms of intergovernmental property rights, the juridical status of the region, etc., while distributional issues are related to the amount of federal income returned to a region from the central budget, in addition to the regional impact of national economic policies.

The third category measures the degree of regionalist political mobilization associated with autonomy-seeking strategies. For regional executives with a more strategic view of the federal bargaining game, holding early elections and popular referenda added democratic legitimacy to their claims while at the same time demonstrating their grip on the internal political situation in their regions, which has been a powerful bargaining chip vis-à-vis Moscow. Likewise, support by the executive for "strong region" parties, for which various aspects of regional autonomy and regional development are central points on the agenda, has been an indication of a regional executive's commitment to the regional autonomy project – especially when doing so meant not openly supporting the "party of power."<sup>251</sup>

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<sup>251</sup> Due to regional leaders' desire to strategically position themselves for all electoral contingencies, "fence-sitting" has been a common phenomenon, where governors will appoint various regional officials to join several parties with prospects for victory. In order to control for this behavior, this part of the index will also be substituted with a weighting based on the actual vote for regionalist parties as well. In the 1999 parliamentary elections, a weight of 2 is given for shares of votes in a region that are 1.25 times higher than the national average for Vsyá Rossiá, 1 from .75-1.25, and 0 for less.

The index is a “snapshot” of the various waves of assertive regionalism and is weighted to take into account differences in preference intensity and timing.<sup>252</sup> It does not purport to capture all types of regionalism, in particular instances of “creeping autonomy” (agency costs), whereby regions appropriate policy authority, economic assets, etc. without challenging the center.<sup>253</sup> Instead, it focuses on assertive regionalism within the context of the federal bargaining game, where the consent of the federal center is necessary to alter the formal rules of intergovernmental relations, and fiscal and economic policy toward the region.<sup>254</sup>

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<sup>252</sup> As noted in chapter 3, during the wave of “republic” declarations from 1991-1993, for instance, a handful of regions actually raised their jurisdictional status through acts of regional legislatures, while a much broader group issued declarations of intent (e.g. plans to hold referenda, deliberation, etc.). The signaling of intent is weighted less than actually following through. Regional executives who took the leading role in various forms of assertiveness generally faced greater uncertainty regarding the federal center’s response than those who followed in their footsteps. Likewise, various groups of regions held elections at different times, with some regions acting as pioneers in the process of sub-federal democratization.

<sup>253</sup> Measuring various agency problems in the policy process (e.g. shirking, information asymmetry) and the ineffectiveness of federal bureaucratic oversight across all the wealthy regions is beyond the scope of the dissertation. See Stoner-Weiss, 1999, for case studies of national policy fragmentation.

<sup>254</sup> Only public actions are counted in the index since these are necessarily known to the federal center, even if it chooses to ignore them.

Table 4.4: Index of Regional Assertiveness

<i>Jurisdictional</i>	<p><u><i>Unilateral Upgrading of Juridical Status (1990-1993)</i></u>  +2 Region declares “republic” status; <i>or</i>  +1 Region threatens to declare only; <i>or</i>  +0 No public declaration/threat</p> <p><u><i>Bilateral Power-sharing Treaties: Signing and Annulment (1994-2002)</i></u>  +2 Signing of treaty; region resists annulment by July 2002 deadline imposed by Moscow; <i>or</i>  +1 Signing of treaty; region rescinded treaty by July 2002 deadline; <i>or</i>  +0 No signing of agreement</p> <p>+1 <u><i>Early Treaty Signing (First wave: 1994-1995)</i></u></p> <p>+1 <u><i>Labeled as a “problem region” by the Kremlin, 2002</i></u><sup>255</sup></p>
<i>Fiscal Redistribution</i>	<p><u><i>“Battle of the Budgets” 1992-1993</i></u>  +2 Successfully implemented single-channel tax status; <i>and</i>  +1 Each instance of “tax revolt,” summer 92&amp;93</p> <p><u><i>“Regional Economic Revolt”: 1996-98</i></u>  +2 Region maintained privileged fiscal status  +1 Economic Revolt: public threat of withholding tax transfers or policy ultimatum issued to federal center</p>
<i>Political Mobilization in Support/ Defense of Autonomy</i>	<p><u><i>Early Elections (1991-1995)</i></u>  +2 Election of regional executive in 1991; <i>or</i>  +1 Election prior to 1995-1996 federal cycle (12/93 – 12/95); <i>or</i>  +0 Election after 1995-1996 federal cycle (9/96+)</p> <p>+1 <u><i>Referendum on Region’s Status in Federation (1992-1994)</i></u></p> <p><u><i>Collective Assertion: Formation of Regionalist Parties (1995; 1999 elections)</i></u>  +2 Governor on political council of party with distinct regionalist agenda; <i>or</i>  +1 Overt identification of governor with regionalist party;  <i>or</i>  +0 “Fence-sitting” or no association with regionalist party</p>

<sup>255</sup> Certain regions were identified by the Kremlin as “problem regions” due to their particular defiance of the Kremlin’s campaign to phase out the treaties, including Sverdlovsk, Kaliningrad, Bashkortostan, Tatarstan, Moscow, and St. Petersburg according to the head of the main legal directorate of the President, Larissa Brycheva on 19 February 2002.

## Control Variables

### *Macrostructural variables*

Table 4.5 highlights the control variables used in the model. The first set of control variables encompasses macro-structural factors, including per-capita GRP (gross regional product), the degree of agricultural output in a region, and geographic factors such as proximity to international markets. According to modernization theory, higher levels of socioeconomic development lead to more sophisticated demands from society in terms of self-governance, encouraging democratization.<sup>256</sup> More developed regions should be more apt to demand greater autonomy from the federal center. Even in advanced democracies such as Western Europe, regions with higher per-capita GRP have been found to exhibit more assertive behavior.<sup>257</sup> Conversely, industrialized regions that also have large agricultural economies might be more dependent on federal subsidies.

In addition, economic geography might play a large role, particularly in terms of border regions. Apart from Kaliningrad, a Russian enclave in northern Europe, the Russian Far East macro-region is the best situated for acting as a portal to international trade, in this case from Eastern Asia. If spatial factors (proximity to foreign markets) do

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<sup>256</sup> See, for instance, Adam Przeworski and Fernando Limongi, "Modernization: Theories and Facts" *World Politics*, 2 (January 1997): 155-183.

<sup>257</sup> On the relationship between economic development and assertiveness, see Milica Zarkovic Bookman, *The Political Economy of Discontinuous Development: Regional Disparities and Inter-regional Conflict* (New York: Praeger, 1991). For an excellent literature review (and empirical test) of economic factors and regional assertiveness in Europe, see Pieter van Houton, "Regional Assertiveness in Western Europe: a Statistical Exploration," a paper prepared for the meeting of the Laboratory in Comparative Ethnic Processes, Duke University, 21-23 April, 2000.



play a large role in regional economic assertiveness, then the dummy variable for Far Eastern *oblasts* should be positive.<sup>258</sup>

### *Fiscal Federalism*

The next set of control variables includes aggregate measurements of the economic and fiscal incentives for assertive behavior within the region itself, including the presence of exportable natural resources in a region, the size of a region's industrial base, and the degree of a region's budgetary dependence on Moscow. According to the literature on fiscal federalism, the first two factors should be positively correlated with assertive regionalism.<sup>259</sup> The latter factor, however, should be negative. Regions that are less dependent on Moscow would have more to gain from pursuing autonomy than those that benefit from fiscal centralization (e.g. the center's ability to collect more revenue from self-sufficient regions and distribute it to poorer regions).<sup>260</sup>

### *Political Resource Mobilization*

The third set of variables measures political-institutional factors that affect regional behavior. Status as an "autonomous ethnic republic" within the Russian Federation inherited from the multi-tiered Soviet ethnofederal structure has been identified in the literature as the most powerful predictor of regional assertiveness due to

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<sup>258</sup> See Michael Keating, *The New Regionalism in Western Europe: Territorial Restructuring and Political Change* (Cheltenham: Edward Elgar Press, 1998).

<sup>259</sup> See, for instance, Krasnick, 1986.

<sup>260</sup> In the German case integration with the European Union has caused the more competitive Lander in the West to clamor for greater fiscal and economic autonomy while the more disadvantaged Lander in the East have been seeking greater engagement by the national government (redistribution). See Arthur Benz, "From Unitary to Asymmetric Federalism in Germany: Taking Stock after 50 Years," *Publius: The Journal of Federalism* 29: 4 (Fall 1999), 55 and Richard Deeg, "Economic Globalization and the Shifting Boundaries of German Federalism," *Publius: The Journal of Federalism*, 26:1 (Winter 1996), 27-52.

the wave of national self-determination that accompanied democratization in the FSU. In particular, Russia's "internal republics" occupied a privileged position in the Soviet hierarchy, providing incumbent leaders with greater political and institutional resources as well as a vested interest in maintaining this special status.<sup>261</sup>

In addition, some non-ethnic regions (*oblasts and krays*) contained ethnic subdivisions, or autonomous okrugs. Theoretically, the presence of titular ethnic populations could also be a bargaining chip for *oblasts* in pressuring Moscow for autonomy. Indeed, several of the power-sharing agreements signed were actually trilateral, including the federal center, the *oblast* and the autonomous ethnic district within it. However, ethnic districts were not allowed to independently sign power-sharing agreements with the federal center, which is why they are not treated as separate observations in the model.

Population size is also a measure of region's political bargaining power, especially in light of the fact that the federal center was in the weakest position during election cycles, when it depended on regional leaders to manipulate administrative levers to "get out the vote" for Yeltsin and pro-government parties in the Duma.<sup>262</sup> Conversely, a protest-minded electorate could also be considered a bargaining chip that could be used

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<sup>261</sup> Since the subset of wealthy Russian regions tested in the model includes only four ethnic republics (e.g. officially designated homeland of titular ethnic group) compared to 38 predominantly Russian regions (*oblasts*), factors specific to ethnicity, such as language and religious differences, history of repression, relative deprivation, etc., will not be tested in this model. Instead, a dummy variable will control for the distinctions between the ethnic homelands and the other *oblasts*. The significance of language and religious factors in regional assertiveness has already been fleshed out by Treisman, 1997.

<sup>262</sup> See, for instance, Vladimir Popov, "Fiscal Federalism in Russia: Rules Versus Electoral Politics," Working Paper, <http://www.nes.ru/public-presnetations/Papers/Popov.htm>, accessed on December 13, 2002.

against the center.<sup>263</sup> The electoral partisanship variable controls for “red belt” regions, based on a low percentage of votes for Yeltsin in the 1996 elections.

*Elite Continuity:* Regional executives that have a very tight grip on power in their regions would be more readily able to mobilize political and administrative resources independent of national level actors. Executive elite continuity is a proxy for the strength of regional leaders. Those who were in power at the end of the Soviet period (e.g. leadership positions in nomenklatura in 1991) and were able to consolidate their grip on power during the following round of elections (1995-1996 for the majority of oblasts, earlier for republics) could be considered as “regional heavyweights.” During the second part of the index period, such powerful regional executives would be expected to be more assertive, as the credibility of their threats would hold more weight than those with weaker power bases, and would be more vulnerable to “punishment” by the Kremlin at the next elections.<sup>264</sup>

*Prior Assertiveness:* Finally, prior assertiveness is also factored into the index for the 1995-2002 time period. As Treisman notes, the credibility of a region’s threats – and hence its bargaining power – is enhanced by previous instances of assertion and successful resource mobilization.<sup>265</sup> If the likelihood of regional assertiveness is dependent on prior instances of assertion (e.g. reputation building), then this variable should be positive.

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<sup>263</sup> Treisman (1999) demonstrates that voting against the incumbent president and party of power was positively correlated with additional transfers from the federal center.

<sup>264</sup> Dowley (1997) notes that Soviet-era elite continuity is positively related with a higher preference for a decentralized federal system during the 1990-1995 time period.

<sup>265</sup> Treisman, *After the Deluge*, 1999.

### *Industrial Concentration*

In order to control for the possibility that large enterprises in general – not just those defined as national-level enterprises – have a significant effect on regional behavior, a control variable is used that measures the distribution of the top 200 Russian enterprises on a region's territory, a much wider base than those designated as “national-level” above. According to Stoner-Weiss (applying Frieden's modern political economy approach), this variable should be positively correlated with regional assertiveness in that a higher concentration of large enterprises able to “capture” the regional administration promotes collective action and cohesiveness among regional elites, enhancing the alliance's ability to act as a united front in opposition to the center.<sup>266</sup>

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<sup>266</sup> Stoner-Weiss, 1997; Frieden, 1991.

Table 4.5: Control Variables<sup>267</sup>

<b><i>Macro-structural</i></b>	
Per Capita GRP <sup>268</sup> ( <i>PCGRP</i> )	Average per-capita Gross Regional Product, 1995-1999
Agricultural Economy ( <i>Agro</i> )	Ratio of agricultural output to Russian average, 1995
Far Eastern Region ( <i>FarEast</i> )	Dummy variable: coded 1/0
<b><i>Fiscal Federalism</i></b>	
Natural Resources ( <i>NatRes</i> )	Regions possessing reserves of oil, natural gas, precious/non-ferrous metals, or exportable timber: coded 1/0
Industrial Base <sup>269</sup> ( <i>IndBase</i> )	Average industrial output, RUR mln
Budgetary Dependence ( <i>BudDep</i> ) (1995+ only)	Average percent of regional budgetary expenditures financed by federal transfers (FFSR)
<b><i>Political Resource Mobilization</i></b>	
Ethnic Republic ( <i>Republic</i> )	Internal “ethnic republic” status in the Soviet federal system, coded 1/0
“Matrioshka” Region ( <i>Subdivide</i> )	Region contains autonomous ethnic districts, coded 1/0
Population Size ( <i>Population</i> )	1991 Population Size
Electoral Partisanship ( <i>Redbelt</i> )	“Red Belt” Region: coded 1/0 if vote for President Yeltsin in 1996 below 50%
Elite Continuity ( <i>EliteCon</i> ) (1990-2002)	Regional executive held <i>nomenklatura</i> position in 1991 and was popularly elected by 1995: coded 1/0
Prior Assertiveness ( <i>PriorInd</i> ) (1990-1994)	Level of assertiveness for the 1990-1994 Period (based on Table 4)
<b><i>Industrial Concentration</i></b> ( <i>IndConc</i> )	Ratio of average output of enterprises within the top Russian 200 enterprises, RUR mln, to total regional industrial output

<sup>267</sup> Source: Goskomstat Annual Statistical Bulletins, 1995-2001 (Moscow: Goskomstat); *Rossiiskie Regiony -2000, 2001, 2002* (Moscow: Goskomstat); Selected Regional Goskomstat Bulletins

<sup>268</sup> GRP data is only available from 1995 onward; for the first phase of the index (1990-1994), the 1995 level is used.

<sup>269</sup> This variable was also substituted with export earnings and the region’s share of the national tax base, all of which are highly correlated with industrial output (85-95%). Average industrial scores were computed separately for each phase (1990-1994, 1995-2002) of the index.

## REGRESSIONS

The regression analysis is conducted on the wealthier cohort of Russian regions (n=44), which account for the lion's share of big business actors in Russia.<sup>270</sup> I used both variants of the independent variable, in its aggregate form and broken down by sector (see Table 4.3 above). Four variations of the assertiveness index have been run against the set of predictors in tables 4-3 and 4-5. The first regression covers the entire time period under study, 1990-2002. It is important to note that from 1990-1994, most vertically-integrated oil and gas companies were still in the process of consolidating their assets in the periphery. Thus, the second variation carves out the 1995-2002 time period, by which time the process of reorganization of the fuel sector (formation of national-level holdings) had largely been completed. This time period covers the bilateral treaty life cycle through the initial deadline for abrogation in July 2002. It also includes a regional “economic revolt” from 1996-1998 and formation of regionalist parties during the 1995 and 1999 parliamentary elections.

The third and fourth variations are organized according to unilateral and bilateral actions. The former include various forms of fiscal protest, declarations of jurisdictional authority and political mobilization, while the latter represent the bilateral power-sharing treaty life cycle. The unilateral index is further broken down across time to control for the earlier period of the transition, when many oil assets were still in the process of being

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<sup>270</sup> Regions above the median industrial output for Russia's 89 regions during the 1990-2002 time period are included in the model. The only exception is Moscow City, which is considered the financial center in terms of center-periphery relations (e.g. headquarters of Moscow-based financial industrial groups that control national-level businesses). The breakaway republic of Chechnya is not included in the analysis since the situation there rapidly evolved outside the parameters of the federal bargaining game into armed conflict.

integrated into national-level structures. The bilateral agreement process was concentrated almost exclusively in the 1995-2002 time period. The non-ethnic regions are tested separately, since the center generally accommodated ethnic homeland regions more quickly and generously than non-ethnic ones.

Each block of Table 4.6 contains the results for four separate regressions: one for each construction of the independent variable in Table 4.3. For the national-level business variable, t-statistic values are also given to measure variations in their significance (e.g. robustness). For the control variables, only the signs are given in this table (full regression results are listed in Appendices A, B, C and D).

Table 4.6: Summary of Statistically Significant Variables

<b>Variation 1: 1990-2002</b>				
	<i>1. Incentives (NATRAT)</i>		<i>2. Influence (REGRAT)</i>	
	<i>a. Aggregate</i>	<i>b. By Sector</i>	<i>a. Aggregate</i>	<i>b. By Sector</i>
<i>National-Level</i>	-3.725***	<i>Fuel: -4.147*** M/M: -3.029***</i>	-2.420**	<i>Fuel: -2.792*** M/M: -1.845*</i>
<i>Control Variables</i>	<i>EliteCon/+** IndConc/+** Republic/+* FarEast/+*</i>	<i>PCGRP/+** Republic/+** FarEast/+** EliteCon/+** IndConc/+**</i>	<i>Republic/+*** EliteCon/+** IndConc/+** Population/+*</i>	<i>EliteCon/+*** Republic/+** IndConc/+*</i>
<i>R2/Adj.R2</i>	<i>.834/.763</i>	<i>.873/.812</i>	<i>.779/.683</i>	<i>.805/.710</i>

**Variation 2: 1995 - 2002**

	<i>1. Incentives (NATRAT)</i>		<i>2. Influence (REGRAT)</i>	
	<i>a. Aggregate</i>	<i>b. By Sector</i>	<i>a. Aggregate</i>	<i>b. By Sector</i>
<i>National-Level</i>	-3.468***	<i>Fuel:</i> -3.907*** <i>M/M:</i> -2.409**	-2.323**	<i>Fuel:</i> -2.340** <i>M/M:</i> -1.945*
<i>Control</i>	<i>EliteCon/+**</i> <i>Republic/+**</i> <i>FarEast/+*</i> <i>Subdivide/+*</i>	<i>Republic/+**</i> <i>EliteCon/+**</i> <i>Subdivide/+*</i>	<i>Republic/+***</i> <i>EliteCon/+**</i> <i>IndConc/+*</i> <i>Population/+*</i>	<i>Republic/+***</i> <i>EliteCon/+**</i> <i>Population/+*</i>
<i>R2/Adj. R2</i>	.791/.700	.803/.709	.746/.636	.754/.635

**Variation 3: Unilateral Actions Only (all expect Bilateral Treaty Cycle)**

	1990-1994		1995 -2002	
	<i>1. NATRAT</i>	<i>2. REGRAT</i>	<i>1. NATRAT</i>	<i>2. REGRAT</i>
<i>National level (b)</i>	<i>Fuel:</i> -0.842 <i>M/M:</i> -1.950*	<i>Fuel:</i> -1.053 <i>M/M:</i> -1.825*	<i>Fuel:</i> -3.379*** <i>M/M:</i> -2.531**	<i>Fuel:</i> -3.221*** <i>M/M:</i> -2.225**
<i>Control</i>	<i>Republic/+***</i> <i>IndConc/+**</i> <i>NatRes/+**</i>	<i>Republic/+***</i> <i>IndConc/+**</i>	<i>EliteCon/+**</i> <i>BudDep/-**</i> <i>Republic/+*</i> <i>FarEast/+*</i> <i>Population/+*</i> <i>PriorInd/+*</i>	<i>EliteCon/+**</i> <i>FarEast/+**</i> <i>Population/+**</i> <i>Republic/+*</i> <i>Agro/-*</i>
<i>R2/Adj.</i>	.732/.628	.747/.649	.793/.681	.808/.704

**Variation 4: Bilateral Actions (Treaty Signing and Annulment)**

	<i>1. Incentives (NATRAT)</i>		<i>2. Influence (REGRAT)</i>	
	<i>All Regions</i>	<i>Non-ethnic only</i>	<i>All Regions</i>	<i>Non-ethnic only</i>
<i>National-Level (b)</i>	<i>Fuel:</i> -1.994* <i>M/M:</i> -1.526	<i>Fuel:</i> -2.705** <i>M/M:</i> -1.928*	<i>Fuel:</i> -1.428 <i>M/M:</i> -0.872	<i>Fuel:</i> -1.498 <i>M/M:</i> -1.335
<i>Control</i>	<i>Republic/+***</i> <i>Population/+*</i> <i>Subdivide/+*</i> <i>IndConc/+**</i>	<i>Population/+*</i> <i>Subdivide/+*</i> <i>IndConc/+**</i> <i>PCGRP/+**</i>	<i>Republic/+**</i> <i>Population/+*</i>	<i>Population/+*</i> <i>Subdivide/+*</i> <i>PCGRP/+**</i>
<i>R2/Adj.R2</i>	.665/.486	.527/.250	.625/.425	.455/.138

\*=significant at the p<0.1 level (90% confidence interval, two-tailed)

\*\*= significant at the p<0.05 (95% confidence interval, two-tailed)

\*\*\*=significant at the p<0.01 level (99% confidence interval, two-tailed)



## Model Results

Among the control variables, two stand out as being the most consistently correlated with higher levels of regional assertiveness across the variations: ethnic republic status and elite continuity.<sup>271</sup> Likewise, per-capita GRP, population size, level of industrial concentration, proximity to international markets (FarEast), and prior levels of assertion were all positive and significant in one or more variations. Conversely, greater dependence on federal transfers for expenditures and a larger agricultural sector (which also depends heavily on federal subsidies) were negatively correlated with assertiveness. All these findings are in line with the literature on assertive regionalism and bargaining in federal systems.

In the first two variations, the proxies for both the stakes of national-level businesses (*NATRAT*) and their relative level of influence (*REGRAT*) in a given region were significant and negatively correlated with regional assertiveness. The higher the relative weight of a region in total national level business output, the lower its level of assertiveness. Likewise, regions which had higher proportions of national-level business output in their economies were less assertive. This supports the thesis that national-level business actors have reduced economic incentives and political opportunities for regional assertiveness.

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<sup>271</sup> Regional leaders that retained their Soviet-era dominance over the political, administrative and financial resources and were able to win the first round of elections enjoyed greater bargaining power (and hence rational expectations of accommodation) than their neighbors with less secure power bases and less effective political machines. For a weaker leader that could face serious competition from rival regional elites, loyalty to the center would be a more rational strategy for staying in power. This may explain why the Kremlin has placed increasing emphasis on influencing the outcome of subnational elections: engineering “regime change” in problem regions has been one of the more effective responses to assertive regionalism by the Putin regime.

In general, the *NATRAT* variable is the more robust (according to t-values) of the two. Incentives for national-level businesses to counter assertive regionalism – based on the stakes involved, or the relative importance of a given region in the total output of national-level businesses – seem to be somewhat more weighty than the relative level of influence in a certain region. Indeed, political influence in a particular region is basically latent without incentives to wield it.

Dividing national-level business actors by sector reveals that fuel assets (*Fuel*) had a stronger effect than did metals and machine-building (*M/M*), which likely stems from the fact that throughout most of the index period, the oil and gas sector was vertically integrated while the metals and machine-building sectors were more fragmented. As the country's "cash cow" the fuel sector was the first on federal politicians' list in terms of consolidation and closely guarded against regional fragmentation.

The third variation captures the difference across time, from the 1990-1994 to the 1995-2002 period. The most important finding here is that the wave of national-level business expansion in the first half of the 1990s mattered for Russia's federal system. For the fuel sector (*Fuel*), neither *NATRAT* nor *REGRAT* are significant in the first period due to the importance of structure: during this time the fuel sector was for the most part still regionally fragmented and not vertically integrated. The only national-level business in the fuel sector that was fully formed during this period was the state natural gas monopoly, Gazprom. By 1995, most of the national-level oil companies had been formed, giving the center additional leverage in certain fuel producing regions, and a

greater interest in using it. Conversely, the first echelon machine and metal enterprises (*M/M*) that remained intact from the Soviet period had a statistically significant effect during the first period, although they were slightly more robust in the 1994-2002 time period. The starkest change, however, is in the *Fuel* component of the national-level business variables; the vertical integration of the energy sector also acted as a political integrating mechanism in Russia's federal system. The fourth variation indicates that the *NATRAT*, rather than *REGRAT*, had an effect on the agreement signing process. The effect is strongest on the *oblasts*, which were unable to use the "ethnic card" as the republics did to pressure Moscow.

Also important is the fact that the *IndConc* variable is significant in several regressions and always positive. Conventional wisdom holds that a greater concentration of big business actors enhances incentives and opportunities for assertion, inasmuch as political and economic elites maintain a united front in exerting rent-seeking pressure on Moscow.<sup>272</sup> While the relationship between higher concentrations of large enterprises and greater regional assertiveness was demonstrated in the regression analysis, there was a *change* in the sign, from positive to negative, as the field of enterprises was narrowed from the wider set of Russia's top 200 enterprises (*IndConc*) to the national-level businesses included in the independent variable (*NATRAT*, *REGRAT*).

This supports the thesis that relative size and structure matter. Even among larger businesses, there are important distinctions. Those that are strategically important in the national economy will have a restraining effect on regional behavior, while businesses

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<sup>272</sup> See for instance, Stoner-Weiss, 1997; Dowley, 1998; Frieden, 1991; Solnick, 1999; Treisman and Schliefer, 2000.

which are important on a regional scale, but not on a national one, have to rely primarily on the regional administration for their rent-seeking objectives. This, in turn, makes them more ardent supporters of assertive strategies aimed at increasing regional regulatory authority (e.g. privatization and bankruptcy) and control over financial resources needed to protect them from take-over by national-level rivals.

### **PATTERNS OF REGIONAL STRATEGIES**

Table 4.7 classifies the wealthiest portion of the regions included in the regression analysis in the previous chapter (all 5 republics and the upper half of the *oblasts*) according to the unilateral and bilateral sections of the index.<sup>273</sup> The rows indicate the overall level of unilateral assertiveness, including jurisdictional declarations, economic protests and regionalist political mobilization, while the columns reflect the bilateral treaty life cycle, including initial signing under Yeltsin and then subsequent compliance with Putin's campaign to enforce federal legislation mandating abrogation of the treaties by July 2002.<sup>274</sup> Ethnic republics are italicized. Regions with asterisks had medium to high levels of national-level business penetration on average across the entire index

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<sup>273</sup> The overall sample used in the quantitative analysis here is 44 regions (5 republics and 39 *oblasts*), or the upper half of Russia's 88 regions ranked by per-capita industrial output, excluding war-torn Chechnya and Moscow City (see fn 270).

<sup>274</sup> The signing of bilateral power-sharing treaties is considered as an act of regionalist assertion due to the ad-hoc nature and asymmetrical outcome of the treaty-signing process in terms of intergovernmental rules; the initiative clearly came from below, and although there were some elements of fiscal harmonization that were advantageous to the center, most treaties centered on privileges specific to a given region. Essentially the treaty-signing process was seen as a stop-gap measure to stem the rising tide of assertive regionalism (Gubogolo, 1997). At the same time, a certain level of regional assertion is necessary in well-balanced federal system, to offset the natural tendency of the federal center to encroach on regional competencies and to more effectively deal with specific local issues.

period.<sup>275</sup> The gray-shaded area indicates a zone of cooperative-type federalism, with relatively lower levels of unilateral assertiveness combined with treaty-signing under Yeltsin followed by compliance under Putin.

Table 4.7: Index Results for Republics and Upper Half of *Oblasts*<sup>276</sup>

<i>Bilateral Treaties</i> <i>Unilateral Assertiveness</i>	<i>Sign / Non-Compliance (2)</i>	<i>Sign / Compliance (1)</i>	<i>None Signed (0)</i>
<i>Very High (8-9)</i> ----- <i>High (5-7)</i>	<i>Bashkortostan</i> <i>Tatarstan</i> ----- <i>Yakutia*</i> , Sverdlovsk, Irkutsk	----- St. Petersburg <i>Komi</i>	----- Maritime
<i>Medium (3-4)</i>	Krasnoyarsk* <i>Udmurtia*</i>	Chelyabinsk* Nizhny Nov.* Vologda*, Omsk*	Kemerovo
<i>Low (0-2)</i>	---	Perm*, Samara* Orenburg* Yaroslavl*, Rostov Krasnodar	Tyumen* Lipetsk* Volgograd Moscow <i>oblast</i>

*Italics* = “Ethnic Republic”

\*= Medium to high levels of national business penetration (over 20%) on average for the entire period, based on both *REGRAT* and *NATRAT* variables

The inverse relationship between national-level business penetration and assertiveness illustrates the results of the regression analysis just presented. With the

<sup>275</sup> Based on the *REGRAT* variable, averaged across 1995-2002. The lower boundary for classification as “medium to high” is 20% (the highest value in the “lower” category is 15%; the lowest value in the “medium to high” category is 22%.) All the same regions would be included in the wealthiest half of the oblasts according to the *NATRAT* variable as well, though individual rankings would be different.

<sup>276</sup> Certain regions were also labeled as “problem regions” by the Putin administration in 2002, including Sverdlovsk, Bashkortostan, Tatarstan, St Petersburg and Moscow. See Tables 4.4. and 5.2.

exception of Yakutia, an ethnic republic, all the regions listed above with a significant level of national business penetration (e.g. those with asterisks) exhibited low to medium levels of assertiveness. Conversely, with the exception of Yakutia, all the regions exhibiting higher levels of assertiveness had lower levels of national business penetration.

The difference between the ethnic republics and *oblasts* is clearly evident, with the former clustered in the upper left quadrant. At the same time, variation within the subsets can be explained by the national-level business variable. Both Yakutia and Udmurtia were less assertive than the wealthier republics without penetration, Bashkortostan and Tatarstan. For the *oblasts*, a lower level of national-level penetration was not a sufficient condition for higher levels of assertiveness, but it was necessary. Conversely, the majority of “loyal” *oblasts* (low to medium levels of assertiveness) have higher levels of penetration by national businesses, and those that do not could be explained by control variables such as large agricultural sectors (Krasnodar and Volgograd), and other federally subsidized industries such as coal (Rostov and Kemerovo).

On the other hand, macro-structural factors such as the absolute size of the regional economy do not fully explain levels of assertiveness. Table 4.8 lists the top fifteen wealthiest *oblasts* for the index period according to levels of assertiveness. It is apparent that ranking according to economic size alone does not explain variation in assertiveness. This is particularly true of *oblasts* ranked closely together, such as Sverdlovsk (2) and Samara (3), and Irkutsk (9) and Perm (10), which are on opposite

ends of the assertiveness spectrum. These four regions will be examined more closely in the next chapter.

Table 4.8: 15 Wealthiest *Oblasts* Ranked by Assertiveness

<i>Level of Assertiveness, entire period</i>	<i>Fifteen Wealthiest Oblasts (Ranked per Industrial Output)</i>
<i>High (7-10)</i>	Sverdlovsk (2), Irkutsk (9), St. Petersburg (11)
<i>Medium (3-6)</i>	Cheliabinsk (4), Krasnoyarsk (5), Kemerovo (6), Nizhny Novgorod (8), Vologda (12), Omsk (15)
<i>Low (0-2)</i>	Tyumen (1), Samara (3), Moscow Oblast (7), Perm (10), Rostov (13), Orenburg (14)

Returning to Table 4.7, it is also evident that sectoral differences are less important than size and structure (e.g. national vs. regional-level businesses). Oil regions could be highly assertive, such as Tatarstan and Bashkortostan, or relatively passive, such as Tyumen and Perm.<sup>277</sup> Likewise, metal and machine-building regions were distributed across the categories, including Sverdlovsk and Irkutsk among the more assertive *oblasts* and Nizhny Novgorod, Samara and Vologda among the more loyal ones. Significantly, unilateral assertiveness was neither a necessary nor sufficient strategy for formalizing regional autonomy in a bilateral agreement. The gray shaded area in Table

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<sup>277</sup> Although Bashkortostan and Tatarstan are both republics, while Tyumen and Tomsk are *oblasts*, Udmurtia is an example of an oil-producing republic with higher levels of national business penetration (and correspondingly lower levels of assertiveness). Likewise, the difference across time demonstrated in the quantitative analysis indicates that oil was only a constraining factor for *oblasts* after their assets were vertically integrated.

4.7 indicates a zone of cooperative-type federalism: lower levels of unilateral assertiveness combined with central accommodation in the form of treaty signing, followed by regional compliance with the federal law mandating that they be abrogated by July, 2002.<sup>278</sup> In particular, regions in the lower row of this area -- Perm, Samara, Orenburg, etc. -- demonstrated substantially lower levels of assertiveness, yet signed power-sharing agreements along with the majority of regions in the middle and upper rows. Thus, a strategy of loyalty was an alternative avenue to accommodation from the center, in contrast to the more competitive type reflected by Tatarstan, Bashkortostan, Sverdlovsk, Irkutsk, and others in the upper row.

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<sup>278</sup> This “defy vs. comply” variable is based on an amendment to the federal register that the agreement had been abrogated or revised (as reported in *Rossiyskaya Gazeta*).



## **CONCLUSION**

This chapter has used regression analysis to establish a causal link between the relative influence of national-level business actors and regional strategic behavior. The greater the stake national-level businesses have in a region, and the larger their weight in a region's economy, the lower the level of assertiveness exhibited by the region. This supports the thesis that national-level business actors have reduced economic incentives and political opportunities for regional assertiveness. By structuring greater constraint, while also supporting alternative strategies for autonomy-seeking, such as "loyalty" to the federal party of power, national-level businesses have helped to reduce the transaction costs of center-periphery bargaining, acting as a "balancing" force in Russia's federal system. To further support this argument, the next chapter takes a more in-depth look at the process of national-level business expansion in the wealthy regions.

## **Chapter 5: Comparing Patterns of National-Level Business Expansion**

This chapter suggests a way of categorizing the wealthy regions through the prism of the dissertation's political economy framework. Three general typologies of regions are identified, based on the timing of “penetration” by national-level business actors, and ensuing patterns of conflict or cooperation with regional administrations. One category includes those regions that have managed to protect strategic sectors of the local economy from integration into national-level business groups from an early point in the transition and, as such, have had consistent incentives and greater opportunities to pursue assertive strategies across the index period. Another category appears on the opposite end of the spectrum. These are regions where newly formed national-level businesses emerging from the Soviet ministries consolidated their control over key sectors early in the transition and have maintained more or less cooperative relationships with regional administrations. The various carrots offered by these businesses have reduced incentives for assertiveness, resulting in more consistent patterns of restraint and “loyalty” relative to the consistently assertive regions.

A third category includes regions where penetration in a strategic sector occurred at a later point in the transition, and was generally accompanied by more conflictual, or “imperialistic” relations between Moscow-based capital and the region. While these regions have exhibited medium levels of assertiveness, there is evidence that they are gradually converging toward the “loyal” end of the spectrum. As demonstrated below, regional elites have become increasingly accommodative of expansion by national-level actors, partly due to the overall trend of increasing integration of key sectors in the

national economy, and partly due to big businesses' greater emphasis on investment in the “real” economy and corporate social responsibility following the August 1998 financial crisis.

To review, the presence of national-level actors shapes both the incentives and opportunities for assertive strategies toward Moscow. In order to preserve their power base, regional elites have strong incentives to maintain both formal and informal levers of control over strategic enterprises within their jurisdictions.<sup>279</sup> The expansion of outside business actors into a region threatens both of these levers; the replacement of key managers disrupts informal channels between the enterprise and the regional administration, while corporate restructuring and downsizing can sever established inter-enterprise relationships and also impact budgetary revenues. In addition, limiting the influence of national-level business actors in a region serves to keep political power more concentrated within existing regional-level elite groups, depriving the federal center of a potential channel of influence over electoral outcomes.<sup>280</sup> In turn, this increases a region's relative bargaining power, giving the regional executive greater opportunity for assertion and less fear of punishment in the next elections.<sup>281</sup>

For regional administrations, protecting strategic sectors from penetration by national-level business actors, which are heavily reliant on federal patronage, requires assertion of jurisdictional rights, including control over privatization and regulation of

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<sup>279</sup> Gel'man et al, 2003; M. Mendras, “How Regional Elites Preserve their Power,” *Post-Soviet Affairs*, vol. 15, no. 4 (Oct.–Dec. 1999), 295-311; Stoner-Weiss, 1997.

<sup>280</sup> See Natalya Zubarevich, “Prishel, Uvidil, Pobedil? (Krupniy Biznes I Regional'naya Vlast)” *Pro et Contra* 7, No.1 (Winter 2002): 107-119, on the increasing activity of big business in regional elections.

<sup>281</sup> Part of the bargaining power of regional strongmen in the ethnic republics, for instance, stems from their ability to ensure political stability in their respective regions. Interview with Irina Katogoshchina, Russian Academy of Sciences Center for Civilization and Regional Studies, April 2002.

bankruptcy, mergers, acquisitions etc. As demonstrated below, these have been integral parts of broader autonomy seeking strategies. Furthermore, regions that have been successful in keeping strategic assets in the hands of regional elites have also been more assertive in the distributional arena as well, in order to keep important regionally-based enterprises afloat during Russia's transition to the market.

In regions where national-level actors have maintained an established, and generally cooperative, presence since the beginning of the transition, jurisdictional issues were solved via power-sharing settlements between big businesses and the regional administration. In the cases outlined below, the integration of regional enterprises into larger national structures has brought them specific benefits in terms of financial resources, management expertise, expanded markets and additional lobbying power. The injection of outside financial resources, together with the presence of steady informal channels to federal decision-makers provided by big business, can help solve distributional problems and ease the strain of economic adjustment, especially as big business has become more attentive to its image in strategic regions under Putin. At the same time, the presence of powerful national-level actors among regional constituents serves to constrain support for assertion "from below," inasmuch as assertive regionalism could disrupt vital relations with federal patrons and has often been associated with more populist, distributive economic policies.<sup>282</sup>

The chapter is organized as follows. It begins by constructing three general categories of regions based on the level of national business penetration and the regions'

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<sup>282</sup> See Chapter 3 for a description of various economic agendas associated with regional assertiveness.

corresponding strategic behavior throughout the entire index period. It then proceeds into a description of representative regions in each category, focusing on Sverdlovsk in the “consistently assertive” category, on Perm and Samara in the “consistently loyal” category, and on Irkutsk as an example of declining assertiveness. Other regions are also briefly mentioned for the sake of comparison and contrast. Instead of a continuous case study, the narrative highlights certain time periods that are important to understanding the nature of national-level business penetration in a given region.

### **CHANGE AND CONTINUITY IN REGIONAL BEHAVIOR**

Table 5.1 categorizes the ten wealthiest regions that signed power-sharing treaties with the federal center, which allows for a more precise comparison of regional behavior across time, since only the regions that signed power-sharing treaties in the 1990s (see Table 4.7, left two columns) could be in defiance of the federal mandate that they be annulled or renegotiated by July 2002. The rows depict the level of assertive behavior during the second phase of intergovernmental relations under Yeltsin, from 1994-1999, which takes into account the vertical integration of the fuel sector during the early nineties.<sup>283</sup>

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<sup>283</sup> By carving out the 1994-2002 part of the assertiveness index from the previous chapter (Table 4.4), the first wave of national-business expansion is better taken into account, especially for the *oblasts*. By 1996, when the *oblasts*, which are the primary focus of this chapter, began to sign power-sharing treaties with the federal center, most national-level energy companies had completed the integration of regional assets into their corporate structures. See, for instance, the examples of Perm and Samara below.

Table 5.1: Behavior across Time of Ten Wealthiest Regions with Power-sharing Treaties<sup>284</sup>

<i>2001-2002: Comply or Defy</i>	<i>Non-compliance with federal mandate by deadline<sup>285</sup></i>	<i>Compliance with federal mandate by deadline</i>
<i>Assertiveness, 1994-1999</i>		
HIGH, 3 -5	Tatarstan Bashkortostan Sverdlovsk Irkutsk	St Petersburg
MED-LOW, 0-2	Krasnoyarsk*	Perm*. Chelyabinsk* Nizhny Nov.* Samara*

\*= medium to high levels of national-business penetration on average for 1994-2002 period: NATRAT or REGRAT score over 20%.

The columns identify the outcome of the Putin administration's success in enforcement of the federal mandate. Regions denoted by asterisks had medium to high levels of national-level business penetration on average throughout the entire index period.

<sup>284</sup> The dissertation is not able to measure the type of agreement signed and its relative value to the region. However, regions such as Samara, Krasnodar, St Petersburg, Komi etc., that were in the compliant group signed treaties giving them wide-ranging autonomy and special privileges on par with Irkutsk and Sverdlovsk in the defiant group. See Guboglo, 1997 and Lisenko, 1998. The main difference is in the *timing*, with the assertive group being accommodated substantially earlier than the loyal group on average. The "quieter" regions that were rewarded for their loyalty under Yeltsin could be expected to resist the central government's attempts to revoke their autonomy alongside the more assertive ones that pioneered the drive. In fact, this did occur for a certain period of time. Almost all of the wealthy regions – from both the "assertive" and "loyal" camps – banded together to resist the mounting trend toward political and fiscal recentralization that appeared on the heels of the August 1998 financial crisis (All-Russia party). However, not long after Putin's electoral victory the Kremlin launched its centralization campaign, and the wealthy regions eventually split into "defiant" and "loyal" camps in the same manner as before.

<sup>285</sup> According to federal legislation passed in 1999, the deadline for renegotiation or abrogation (which was the Kremlin's preferred outcome) of the power-sharing treaties was end-July, 2002. The data is based on the official timing of treaty nullification, as published in *Rossiskaya Gazeta*. This measure captures only the formal outcome of the process, e.g. whether the action was officially recorded as having taken place prior to August, 2002.

Cross-time analysis demonstrates the polarization of the wealthiest regions into two distinct camps, “assertive” in the upper left hand quadrant and “loyal” in the lower right. Across both periods, eight of the top ten regions that signed agreements remained consistent in terms of their level of national business penetration and corresponding strategy, while two deviated during the Putin era. Krasnoyarsk, with a relatively high level of national-level business influence, held out beyond the deadline while St. Petersburg, with relatively low penetration, succumbed to pressure a couple months prior to the deadline.<sup>286</sup>

A closer examination of the 1999-2002 time period reveals an important distinction among the more assertive regions in the upper left cell in Table 5.1. As the deadline was nearing, the Presidential Administration publicized a list of “problem regions,” which were overtly defying the Kremlin and publicly criticizing the federal center’s mandate as an encroachment on regional autonomy. The staunchest defenders of the asymmetrical federal system under Yeltsin included several, but not all, of the same regions that would defy the deadline put forth in the legislation; however, there were also regions on this list which eventually did comply. The columns of Table 5.2 below measure the outcome of the Kremlin’s campaign to phase out the power-sharing agreements by the initial deadline, which could be structured by a number of factors involved in bilateral negotiations, while the rows measure the region’s initial response, or

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<sup>286</sup> Both cases were in fact linked to changes in the strength of the power base of the regional executive, which is significant and positive in the regressions. St Petersburg was cited as a problem region, but the Kremlin was able to erode governor Yakovlev’s power base through its influence in the city legislature, ultimately dashing his hopes for a third term – something that undermined his bargaining power. On the other hand, the election of Alexander Lebed, a federal politician, in Krasnoyarsk in the late 1990s afforded the region additional bargaining power vis -à-vis the center while he was in office. Saint Petersburg is also Putin’s hometown, which has given it closer federal scrutiny.

stance, in the public political arena to the campaign itself.<sup>287</sup> Regional politicians most zealous of their autonomy would be expected to be the most overtly defiant and vocal in opposition to the threat of federal encroachment.

Table 5.2: Regional Reactions to Legislation on Bilateral Treaty Abrogation (Ten Wealthiest Regions)

	<i>Non-compliance with federal mandate</i>	<i>Compliance with federal mandate</i>
<i>Problem Region</i> <sup>#</sup>	Tatarstan Bashkortostan Sverdlovsk	St Petersburg
<i>“Quiet”</i>	<b>Irkutsk</b> * Krasnoyarsk*	Perm* Chelyabinsk* Nizhny Novgorod* Samara*

<sup>#</sup>Labeled as “problem region” by the Presidential Administration, February 2002. The City of Moscow was also listed as a problem region, but it is not included in the study.

\*= medium to high levels of national-business penetration on average in 2000-2002: NATRAT or REG RAT score over 20%. Irkutsk passed this threshold in 2001.

When both aspects of the agreement annulment process are examined, the distribution of regions within the Putin period remains exactly the same as in Table 5.1 with one exception: Irkutsk (marked in bold) falls out of the highest category of assertiveness in the upper left quadrant. During the second wave of national business expansion from 2000-2002, Irkutsk’s economy increasingly fell under the control of

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<sup>287</sup> Measuring a region’s unilateral response better pinpoints the most defiant regions. Bilateral negotiations could drag on beyond the deadline due to a number of external factors, such as the timing of regional elections, as in the case of Yakutia.



national-level business groups. Accordingly, after 2000, both its *NATRAT* and *REGRAT* values increased from the “low” to “medium” categories. Like Krasnoyarsk, Irkutsk deviated from the staunchest assertive regions in the Putin period.<sup>288</sup>

Based on these observations, Table 5.3 outlines three main categories of intergovernmental relations. The first and second categories can be envisioned as certain points on a spectrum based on observed behavior across the Yeltsin and Putin periods, from less assertive, or consistently “loyal” on one end to consistently assertive on the other.<sup>289</sup> The third category represents regions that have moved along the spectrum over time; the overall direction of the movement has been from the assertive to the loyal end.

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<sup>288</sup> Both Irkutsk and Krasnoyarsk were oblast pioneers in terms of petitioning for republic status back in late 1991. Irkutsk in particular was also consistently assertive in the Yeltsin period, matching Sverdlovsk in terms of earlier treaty-signing and (along with Krasnoyarsk) gubernatorial elections (i.e. before the June 1996 presidential elections), tax revolts in 1997 and support for a regionalist party leading up to the 1999 Duma elections (in the case of Irkutsk, *Vsya Rossiya*). See Chapter 3 for more details.

<sup>289</sup> It is important to note that the extent of a region’s “loyalty” is relative to the actions of its assertive neighbors and the existing norms of center-periphery interaction, and may not necessarily indicate satisfaction with the existing federal arrangement. For regional executives, remaining “quieter” may be considered a strategy of loyalty when other regional leaders are pursuing assertive strategies. In times where the center takes the offensive, loyalty is reflected in acquiescence to central mandates. As shown earlier, the ends pursued via a strategy of loyalty can be the same as those pursued by strategies of assertiveness – accommodation by the center – but the means, and therefore the qualitative nature of intergovernmental relations, are profoundly different in this case. A strategy of loyalty is based on expectations of reciprocity, in that the region expects to be rewarded at a later point, while assertive strategies are based on unilateral actions and threats to coerce the center into accepting the region’s terms and timing.

Table 5.3: Categories of Wealthy Regions Based on Timing of Penetration

<i>Category</i>	<i>Representative Region</i>	<i>National – Level Penetration</i>	<i>Timing of national-level business expansion</i> <sup>290</sup>
Consistently Assertive	Sverdlovsk	Low	Low levels of penetration through 2002
Consistently Loyal	Perm, Samara	Medium, High	Significant penetration during <i>first wave</i> , 1990-1996
Declining Assertiveness	Irkutsk	Low increasing to Medium	Significant penetration during <i>second wave</i> , 1999-2002

The selection of these four regions controls for other variables affecting regional behavior. In terms of economic potential, Sverdlovsk and Samara have similarly large and diversified economies, taking second and third place among all the Russian regions, while Irkutsk and Perm are ninth and tenth largest, respectively. Likewise, in order to control for republic status (e.g. status as a titular ethnic homeland), which is significant and positive in all the regressions, only the non-ethnic regions listed in Table 5.2 will be the primary focus of the comparative study below. The second control variable that is robustly positive in most regression variations is executive elite continuity, which is evenly distributed across these four regions: Sverdlovsk and Samara have demonstrated executive elite continuity across the entire index period while Irkutsk and Perm have not.<sup>291</sup> At the same time, examples of other ethnic republics and *oblasts* listed in table 4.7 will be cited at certain points for the sake of comparison and contrast.

<sup>290</sup> This column measures a significant change in the level of penetration, from low to medium/high (*REGRAT* or *NATRAT* above 20%).

<sup>291</sup> There were brief intervals when regional leaders were sacked by Yeltsin in 1993, only to return to power during the first round of gubernatorial elections (e.g. Sverdlovsk, Cheliabinsk, Novosibirsk, etc.) In the case of Sverdlovsk, E. Rossel was sacked by Yeltsin in late 1993, only to return to power in 1995.

## Organization of the Narrative

The narrative is divided into both the Yeltsin and Putin periods. The Yeltsin period covers the “first wave” of national-level business expansion: the formation of vertically-integrated energy companies and initial integration of regional assets from 1992 -1996, followed by the further privatization of state-owned shares in both oil and metals companies by Moscow-based financial-industrial groups during the “shares for loans” auctions surrounding the 1996 presidential elections.<sup>292</sup> Some national-level businesses, such as the oil holdings Lukoil and Surgutneftegaz, remained under the control of the managers and bureaucrats that had facilitated their formation. For the purposes of the dissertation, the share of state control is not as important as the actual process of regional expansion, or the nature of relations with the regional administration. This is especially true under the Yeltsin administration, when the state was far from being a “hands-on” manager of its assets; the senior management of even the most strategic companies like Gazprom was allowed wide-ranging autonomy and privileges.<sup>293</sup> The transfer of ownership of national-level assets via the highly contested “loans-for-shares”

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<sup>292</sup> The first wave of national-level business expansion under Yeltsin involved the creation of national-level energy companies, including Russia’s two largest corporations – Gazprom (natural gas) and United Energy Systems (electricity) – at the very beginning of the transition. The next step was the creation of national-level oil companies: from late 1992-1995, the controlling interests of 30 oil-extracting and 28 oil-refining companies dispersed across various regions were consolidated within ten state oil holding companies, each of which met the size and structural criteria for national-level enterprises. The oil sector was first consolidated as early as 1991, including *Lukoil* and *Surgutneftegaz*. Gazprom was also privatized in this phase. This was followed by a series of presidential decrees from November 1992 to April 1995, setting up *Yukos* (1993), followed by *Slavneft*, *Eastern Oil Company* and *ONACO* in 1994 and then *Rosneft* and *TNK*, *Sidanco* in April 1995. In addition, *Rosneft* and *Transneft/Transneftprodukt* remain state-run companies. See Lane, 1998.

<sup>293</sup> For instance, Russia’s chief architect of privatization in the first half of the 1990s, Anatoly Chubais, remarked that during 1993, only five of 150,000 state enterprise directors were removed from their posts, even though abuse of state assets was widespread. Yelena Kotelnikova, “Meeting of the Government Presidium: Private Owners Will Officially Run State Enterprises,” *Kommersant-Daily*, May 20, 1-2, *CDSP*, Vol XLVI, No.20 (1994), 10.

auctions in the second phase did matter, however. As demonstrated below, acquisition of national-level businesses by Moscow-based financial-industrial groups (FIGs) often led to large-scale corporate restructuring, changes in regional management and corporate tax homes, all of which disrupted existing relationships between the enterprise and the regional administration.

The post crisis period, which falls under Putin's presidency, includes the “second wave” of national business expansion following the August 1998 financial crisis.<sup>294</sup> During this time, the lion's share of strategic enterprises in the metals sector was consolidated into national-level businesses. This main focus of this period will be the emergence of the third category of regions: those with declining levels of relative assertiveness due to the integration of their strategic assets into national-level businesses.

## **FIRST WAVE OF EXPANSION UNDER YELTSIN**

### **Sverdlovsk and Irkutsk: Resisting Penetration Early On**

Sverdlovsk is indicative of the first category of wealthy regions that have been consistently assertive throughout the index period, while Irkutsk exemplifies the third category, or regions which demonstrated declining amounts of assertiveness due to penetration by national-level business actors under Putin. In order to emphasize the initial similarities between these two regions – mainly their ability to limit national-level business penetration during the first wave of expansion in the early to mid-1990s– they will be discussed together in this section. In addition, this section will also include some discussion of the most assertive ethnic republics, such as Tatarstan and Bashkortostan, in

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<sup>294</sup> Putin was appointed Prime Minister in the fall of 1999 and elected President in March 2000.

order to highlight the similarities in strategies among the ethnic and non-ethnic regions. These ethnic regions served as trailblazers for the assertive oblasts such as Sverdlovsk and Irkutsk.

Sverdlovsk and Irkutsk, along with the other assertive regions in the upper row of Table 5.1, all have two factors in common.<sup>295</sup> First, they did not inherit any first-echelon, or national-level, enterprises (as classified in Table 4.1) from the Soviet era.<sup>296</sup> Second, during the first phase of national business expansion, from 1991-1996, they were able to stave off the penetration of newly forming national-level businesses into their jurisdictions. As a result, throughout the 1990s these governors' business constituencies consisted primarily of regional-level enterprises, allowing them to organize corporatist-type arrangements protecting regional industries in order to preserve the *nomenklatura* ties that underpinned their power base.

Maintaining a "winner-take-all" strategy – attempting to keep the region's strategic economic assets within the hands of the existing regional elite group – required both formal protection from federal encroachment on regional regulatory authority (especially in the spheres of privatization, bankruptcy, etc.) as well as a strong degree of economic self-sufficiency in order to meet the needs of regional enterprises faced with greater competitive pressures from market reform. This, in turn, created incentives for assertion in both the jurisdictional and distributional arenas. With the influence of the

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<sup>295</sup> Irkutsk is included in the first category during the earlier part of the Yeltsin period, since it was gradually "penetrated" at a later period, from 1997-2002.

<sup>296</sup> Sverdlovsk had one very large regional-level enterprise that is classified as borderline – Nizhny Tagil, which is tested both ways. If classified as national-level, it does not change the significance of the coefficients, except that the  $r^2$  decreases by 0.6. The enterprise was eventually integrated into EvrazHolding, which in 2001 entered the first echelon of Russian businesses (see Table 4.1).

third player in the federal triangle – national-level business – minimized in these cases, these issues were mainly decided in the classic two-player game between the federal center and regional governments. Within this context, regionalist political mobilization was used to increase the respective region's bargaining power by adding a stamp of democratic legitimacy to its claims.

### *Jurisdictional Arena: Asserting Control over Privatization*

The outcome of the struggle for control over the privatization of major industrial assets during this phase was the most decisive determinant of a region's ability to sustain strategies of assertiveness.<sup>297</sup> It is important to note that the most assertive ethnic republics set the example for non-ethnic regions. For instance, Bashkortostan and Tatarstan were able to leverage their sovereignty declarations and early presidential elections into the formation of regionally-based oil companies (Bashneft and Tatneft), which were not included in the dozen state holding companies set up by the state from 1992-1995. In addition to the formation of autonomous oil companies, authorities in Tatarstan and Bashkortostan manipulated market institutions to actively discourage participation of outside (Moscow-based) capital in regional companies and restrict key managerial posts to members of the ruling elite group, often relatives of key governmental officials.<sup>298</sup>

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<sup>297</sup> Both Sverdlovsk and Irkutsk were highly assertive during the first and second phases of regional assertion, from 1991-1993 and 1994-1999, respectively. See Chapter 3 for a detailed description of their activities.

<sup>298</sup> In essence, the republican elites aimed to set up statist regimes with a strong degree of governmental control over corporate activity. For instance, in 1993 the Bashkir President intervened when it came to his attention that Moscow-based companies were purchasing large shares in the republic's Uchaly Mining and Concentrating Combine, and bent market rules to close off the company. See Gulchachak Khananova, "An

*Oblast* executives followed suit and asserted control over strategic assets on their territories. The Irkutsk regional administration successfully kept the region's most strategic asset – the *Irkutskenergo* hyrdo-electric power station – from being forcibly integrated into one of the largest national-level business actors, United Energy Systems, the state energy monopoly which was formed by presidential decree in the early 1990s.<sup>299</sup> In addition to jurisdictional assertiveness – Irkutsk was one of the first non-ethnic regions to demand republic status in 1991 – the region's governor, Yuri Nozhikov, took the case to the Supreme Court before Moscow finally acknowledged his claim over the power station.

Sverdlovsk's autonomy project centered on securing control over the non-ferrous sector. From 1990-1991 Rossel won expanded control over foreign trade activity in the region, including the distribution of export quotas and a certain percentage of revenues from raw materials sales.<sup>300</sup> Rossel was able to use this regulatory authority to set up a narrow group of "authorized" non-ferrous metals exporters close to the regional administration. The constitution of the Urals Republic declared in the summer of 1993 afforded the regional government wide-ranging rights over the privatization and regulation of regional industries, similar to that declared by Tatarstan and Bashkortostan.

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Unprecedented Decision by the Bashkir Authorities: the President Authorizes an Open-type Company to become a Closed-type Company," *Kommersant-Daily*, February 7, 1995, *CDSP* Vol XLVII, No. 6 (1995).

<sup>299</sup> The power-generating station is particularly important due to the dominance in the region of aluminum production, which is electricity intensive. Control over the station allowed the regional authorities to maintain lower prices than otherwise would have been possible if prices were set in Moscow, in effect allowing them to subsidize local industry. See Alexsei Tarasov, "Political Power Engineering: Siberians Don't Want to Turn Power Plants Over to the Center," *Izvestiya*, Feb 17, 1993, 5; *CDSP* XLV, No.7, (1993).

<sup>300</sup> "Business, Urals Style," *Current Digest of the Soviet Press*, Vol 42 No.45 (1990), 25.

In particular, it confirmed Rossel's control over foreign trade activity in the region, attempting to formalize the ad-hoc concessions awarded by President Yeltsin earlier.<sup>301</sup>

However, the Urals Republic never came into being. Rossel was dismissed by President Yeltsin in November of 1993 as the Kremlin, in an effort to restore order after the resolution of the Constitutional Crisis, began to crack down on the most assertive regional officials among the *oblasts*. The newly appointed governor of Sverdlovsk, A. Strakhov, promptly initiated a redistribution of ownership within the aluminum sector in an attempt to undermine Rossel's influence over the sector. Only upon winning the right to hold an early election in August 1995 – in which Strakhov was defeated – was Rossel able to reassert control over privatization in the sector, thwarting Strakhov's last-ditch effort to create a holding company uniting the region's aluminum enterprises and then transfer its ownership to a Moscow-based financial group.<sup>302</sup>

The case of Sverdlovsk emphasizes the importance of popular elections for “winner-take-all” autonomy projects: due to the weakness of property rights, changes in executive power often entailed a redistribution of property. Strakhov's attempt to re-subordinate the region's most lucrative sector to national-level business elites (who in

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<sup>301</sup> Rossel used the treaty to consolidate his control over non-ferrous exports, one of the most lucrative sectors in the region. His defeat over Strakhov in the election paved the way for him to re-establish control over the aluminum sector in the months following. Yelena Tregubova, “The Father of the Urals Republic Regains his Governor's Post,” *Segodnya*, Aug 22, 1995, 1, *CDSP*, Vol. XLVII, No. 34 (1995), 14.

<sup>302</sup> Right before the election, the federal government gave Strakhov the right to dispose of the state-owned packages of shares in all enterprises in the Urals aluminum complex. Strakhov hastily transferred the shares to a new holding company, ALKOR (Aluminum corporation), which was bought for a symbolic price by the *Rossiisky Kredit* Financial Group. When Rossel returned to power after the election, he petitioned the prosecutor's office to investigate the transfer, which was eventually reversed. In addition, he vowed to review all privatization decisions in the oblast during his interregnum, intending not as much to reverse the privatization process but to prevent “further transfer of the province's property to Moscow.” See Viktor Smirnov, “Sverdlovsk's Newly Elected Governor, Eduard Rossel: I Will Leave a Province that is a Monument to Independence,” *Kommersant-Daily*, August 26, 1995, 23, *CDSP*, Vol. XLVII, No. 34 (1995).



turn relied on patronage from federal officials) demonstrates that jurisdictional assertiveness is only effective to the degree that the regional executive is insulated from the reach of national-business working through their influence in the Kremlin.<sup>303</sup> The assertive ethnic republics, Tatarstan and Bashkortostan, had managed to hold early elections in 1990/1991, when Moscow was preoccupied with the power struggle between Gorbachev and Yeltsin. Both Nozhikov and Rossel – eager to protect their control over key regional assets – were also two of the most vocal *oblast* lobbyists for holding regional elections.<sup>304</sup>

The assertive regions were also among the pioneers in the power-sharing treaty cycle, with Tatarstan and Sverdlovsk being the first republic and *oblast*, respectively, to sign treaties with the center. The power-sharing treaties were designed to secure their respective region's gains from the first phase of privatization. Thus, Tatarstan's and Bashkortostan's treaties afforded them near total control of privatization over the oil and oil processing sectors on their territories, as well as major regional industries such as Kamaz in Tatarstan.<sup>305</sup> Sverdlovsk's treaty confirmed the regional administration's rights over privatization of various federally owned enterprises, control over foreign trade activity, and set up a regional investment fund from export/mineral taxes that would have

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<sup>303</sup> As a Kremlin loyalist, Strakhov was also under the influence of national-level business interests: the fact that the federal government enabled Strakhov to transfer control over the region's aluminum industry to *Rossiskiy Kredit* – one of the Kremlin's "authorized banks" – right before the elections indicates the influence of national financial interests in the Kremlin's policy toward privatization in the regions. The connection between PM Chernomyrdin and Gazprom, which acquired shares in many debtor enterprises around the country, is one of many other examples.

<sup>304</sup> Nozhikov won the right to hold an election in April 1994, over a year before Rossel did in August 1995. The first round of multiple regional elections (a dozen or so regions) took place in December 1995, followed by the general round of *oblast* elections starting in September 1996.

<sup>305</sup> See Chapter 3 for more details on these power-sharing treaties.

otherwise been beyond the purview of the regional budget.<sup>306</sup> Finally, Irkutsk secured the right to manage the state's 40% stake in Irkutskenergo in its power-sharing treaty.

### *Distributional Arena: Sustaining Localist Corporatist Arrangements*

Regional assertiveness under Yeltsin was not only a function of sheer political opportunism, or entrepreneurial politicians taking advantage of central weakness in order to “steal the state.”<sup>307</sup> In the run-up to the signing of bilateral power-sharing treaties, assertive regional leaders also emphasized the need to control the privatization and regulation of key sectors in order to increase their effectiveness in dealing with the strains of economic adjustment, including cushioning the effect of inflation, protecting large employers, and spurring a recovery in manufacturing amidst the national economic recession.<sup>308</sup> Indeed, assertiveness was accompanied by various forms of statist economic policies – based on local corporatist arrangements, redistribution and regional protectionism – designed to enhance their political base while at the same time shielding key industries from “penetration” by national-level rivals.

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<sup>306</sup> Legislation passed by the *oblast* legislature established strict control of the regional administration over privatization, bankruptcy, and changes in board of directors for the region's largest enterprises. This was possible since the power-sharing treaty transferred jurisdiction over many federal enterprises to the regional level. See Victor Smirnov “Governor Rossel Launches Fight With Federal Authorities for Control Over Privatization”, *Kommersant-Daily*, December 16, 1995, 2, *CSDP*, Vol XLVII, No. 51(1995), 23.

<sup>307</sup> The reference here is to Steven Solnick's “Stealing the State,” which focuses on the breakdown of political hierarchies and ensuing agency problems and that accompanied the collapse of the Communist Party of the Soviet Union. Steven Solnick, *Stealing the State: Control and Collapse in Soviet Institutions* (Cambridge: Harvard University Press, 1998)

<sup>308</sup> Smirnov, 1995. Rossel indicated that his goal in lobbying for the transfer of the jurisdiction over enterprises in the region was not only a one-off augmentation of the oblast budget (e.g. privatization proceeds), but also in the longer-term to increase the administration's ability to effectively manage Sverdlovsk's economy.

While varying degrees of state interventionism and corporatist arrangements have been prevalent in most regions, the dominance of regional-level enterprises in these governors' constituencies reinforced trends toward assertiveness in the distributional, as well as jurisdictional, arena. Rather than "sharing" control over regional industry (and thus political influence) with national-level financial-industrial groups, top regional managers and politicians attempted to maintain local cartel-like structures that were primarily financed by regional fiscal resources.

Insulating the regional political economy from national-level businesses carried a heavy price tag, however, and not only in terms of the risky jurisdictional assertiveness (e.g. republic declarations) which got Rossel fired, and nearly Nozhikov.<sup>309</sup> The financial burden of clearing up the vicious circle of non-payments in industry – especially wage arrears, which were the most politicized – and scraping up funds for investment into manufacturing was substantial, even for the wealthy regions. Local resources and policy discretion alone were not sufficient to deal with the extent of the industrial decline during the 1990s.<sup>310</sup> Thus, even after gaining as much control as possible over privatization, natural resource rents, taxation, and corporate governance and restructuring within their jurisdictions, regional executives also endeavored to wrench back fiscal resources from the common (federal) pool.

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<sup>309</sup> Rossel was removed in November 1993 due to his vigorous pursuit of an independent "Urals Republic" in the region. See Chapter 3 for more details.

<sup>310</sup> According to an elite survey conducted by the Russian Academy of Sciences, regional executives tended to blame Moscow for not doing enough to deal with the nationwide economic decline. See "*Rossiia: Tsentr i Regiony (Russia; Center-Periphery Relations)*" No.2, Institute for Sociopolitical Research (Moscow: Russian Academy Sciences, 1998). In this context, assertive regionalism can be viewed as demonstratively "passing the buck" for the economic hardship.

Thanks to their privileged status as ethnic homelands, Tatarstan and Bashkortostan enjoyed highly preferential tax regimes throughout the Yeltsin era, which left them a disproportionate share of the consolidated tax base. Combined with their jurisdictional gains, this allowed them to closely guard regional assets from outside control, while at the same time stimulating the regional economy.<sup>311</sup> The relative ease in which Mintimer Shamiev and Martuza Rakhimov were re-elected throughout the 1990s – while at the same time maintaining an assertive stance vis-à-vis the Kremlin and Moscow-based capital – attests to their success.<sup>312</sup>

The contrasting stories of Sverdlovsk and Irkutsk are indicative of the mixed success experienced by assertive *oblast* executives in constructing similar arrangements. Edward Rossel in Sverdlovsk was generally successful in building a coporatist-type arrangement that gave the regional government and affiliated financial interests a central role in facilitating inter-enterprise trade and solving corporate finance problems (e.g. settling of liabilities, funds for guaranteed orders) for a privileged group of regional-level enterprises, particularly in the defense and metallurgy sectors.<sup>313</sup>

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<sup>311</sup> Executives in these regions used their control over the privatization process to build patronage networks that gave them excessive influence over businesses in their region. See for instance, S. Peregudov, N. Lapina and S. Semenko, *Interest Groups and the Russian State*, (Moscow: Editorial URSS, 1999), 195-210.

<sup>312</sup> In February 1994, the Prime Minister of Tatarstan, M Sabirov boasted that because of its privileged fiscal status, Tatarstan was able to maintain the lowest prices for bread, milk and dairy products in Russia. Likewise, the Chairman of the Soviet of Ministers of Karelia, S Blinnikov, noted that the preferential share of hard currency receipts left to the republic allowed it to finance several major investment projects (e.g. railroad) and maintain an extensive welfare program, which, if not for the republic's drive for economic sovereignty, would have been "unthinkable." See M Sabirov, "My Vnosim Nalogi v Federal'nyu Kaznu: no Summa Dolzhna byt' Real'noy i Obosnovannoi," *Nezavisimaya Gazeta*, 2 October 1993; S Blinnikov, "Nasha Tsel – Ekonomicheskii Suverenitet," *Delovoy Mir*, 28 Feb - 6 Mar, 1994, 14.

<sup>313</sup> The regional budget acted a clearing center and guarantor for the various financial transactions concerning enterprises the group, in which the administration was often a shareholder. Smirnov, 1995 and Startsev, 1999.

Likewise, Yuri Nozhikov in Irkutsk presided over a localized brand of corporatism, using subsidies, tax incentives and credits to increase the administration's leverage over the main pillars of the regional economy.<sup>314</sup> Irkutskenergo was one of the chief instruments for subsidizing local industry; together with the region's gold deposits, the power station had been the central focus of regional assertiveness in the jurisdictional arena in the early 1990s. Via its stake in the company, the regional administration could maintain prices for local electricity at considerably lower rates than in neighboring regions, which helped to stimulate the region's aluminum industries. By 1997, the power station had come to be the largest creditor to regional industry.<sup>315</sup>

For both regions, however, the finiteness of local resources and the staggering magnitude of industrial debt, coupled with an austere monetary policy at the national level, made it virtually impossible to resuscitate the local economies at the regional level alone, no matter how wide-ranging autonomy jurisdictional autonomy. Thus, in addition to privileges enshrined in the power-sharing treaty, Rossel lobbied heavily for national monetary and industrial policies more conducive for stimulating an economic recovery in the region. Frustrated with the lack of response through traditional channels, Rossel issued a policy ultimatum in February 1997 designed to pressure the center into responding to the needs of domestic manufacturers in the Urals region.<sup>316</sup> Likewise, in March 1997, Irkutsk governor Nozhikov also tried to lobby the Ministry of Finance for

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<sup>314</sup> See Michael Bradshaw, Alexander Chernikov and Peter Kirkow, "Irkutsk and Sakhalin," in Phillip Hanson and Michael Bradshaw eds, *Regional Economic Change in Russia*, (Cheltenham, UK; Northampton, MA: E. Elgar, 2000), 200-205.

<sup>315</sup> Ibid.

<sup>316</sup> Viktor Ivanov, Viktor Smirnov and Denis Dyomkin, "Eduard Rossel Gives Moscow until February 20; Urals and Maritime Territory Stage Economic Revolt," *Kommersant-Daily*, Feb 6, 1997, 2.

additional funds. When his requests fell on deaf ears, he initiated a short-lived tax revolt and threatened to unilaterally implement an anti-crisis program in the region.<sup>317</sup>

Rossel ultimately proved more adept than his Irkutsk counterpart in meeting the needs of his regional-level constituency. Although his grip on political resources in the region was considerably looser than his counterparts in Bashkortostan and Tatarstan, he managed to retain his gubernatorial seat throughout the Yeltsin period. Meanwhile, in Irkutsk the web of non-payments had become such a strain on the regional budget that Nozhikov was forced to resign after it became apparent that the federal government was not going to cave in to his tax revolt, which was viewed as a last-ditch effort to wrench live cash from the center to help alleviate the debts owed regional industries.<sup>318</sup> The failure of Nozhikov's corporatist scheme had instant repercussions: debt-laden enterprises in the local economy became more vulnerable to penetration of Moscow-based capital. In early 1997, the Angarsk refinery was taken over by the national-level oil holding Sidanko. At first, relations between the refinery and regional administration quickly deteriorated, as the refinery implemented a restructuring program and changed management, which reduced the regional administration's leverage over the enterprise as well as the amount of tax receipts flowing into regional coffers.<sup>319</sup>

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<sup>317</sup> Irkutsk's anti-crisis program had much in common with Rossel's, including heavy state intervention (increasing administrative control over the economy), nationalization, currency emission, re-distribution of income from the natural resource sector to manufacturing sector (charging rent, anti-monopoly policy to reduce energy and transport tariffs, etc.). Dmitry Kamyshev, "Irkutsk Secedes From Russia...for a Month, at least," *Segodnya*, March 4, 1997, 1. Dmitry Kamyshev and Irina Nagornykh, "Irkutsk Governor's Tax Revolt is Put Down," *Segodnya*, March 5, 1997, 1-3.

<sup>318</sup> The growing non-payment problem eventually brought about the downfall of the Nozhikov administration: up to half of regional tax base was IOUs, which caused wage delays. Bradshaw et al, 2000, 203-205.

<sup>319</sup> Ibid.

It is important to note that Nozhikov's successor, Irkutsk mayor Boris Govorin, was supported by the same regional-level business constituency as Nozhikov; correspondingly, the region continued to demonstrate assertive behavior in the following years. Furthermore, Govorin and Sidanko eventually came to terms over the Angarsk refinery. Nevertheless, after Nozhikov's failure and the Angarsk refinery takeover the regional administration's influence and power base had narrowed considerably, which opened the door for a more significant expansion of national-level enterprises in the region during the 1999-2002 time period, as demonstrated below.

### **Earlier Penetration: "First Wave" Regions**

This section will focus on the consistently loyal regions, Perm and Samara. In these regions, corporatist-type arrangements between the regional administration and national-level businesses helped to structure more stable federal relations. In contrast to the "winner-take-all" strategies evidenced above, these models are indicative of "power sharing" arrangements with national-level business actors. Both jurisdictional and distributional issues were primarily solved along the second segment of the federal triangle – between national-level businesses and the regional administration – reducing the need for more costly assertive strategies vis-à-vis Moscow, as has been the case with the consistently assertive category. For the sake of contrast, the second part of this section will briefly highlight two other regions, Udmurtia and Krasnoyarsk, where penetration was less cooperative and more contested.

*Big Business as a Carrot: Perm and Samara*

In Perm, the process of integration of the region's various oil companies into the Lukoil holding began in the early 1990s, culminating with the formation of Lukoil-Permneft and a group of smaller associated enterprises.<sup>320</sup> Lukoil's consolidation of oil and petroleum product assets in the region was hardly the case of a "hostile" takeover: plans for integration of regional oil assets into Lukoil enjoyed support from local economic managers whose companies were threatened by the precipitous decline in production throughout the economy.<sup>321</sup> While the regional administration could provide tax relief and various incentives to stimulate production, the scope of the problem went far beyond the region's financial capabilities and jurisdictional boundaries. Perm's fuel companies were located on the periphery of the traditional Soviet oil sector, which was concentrated further to the east, in Western Siberia. Having been relatively neglected by Soviet planners and somewhat isolated geographically (in terms of the main oil distribution routes), the region's enterprises were in need of heavy capital investment, and in particular access to broader markets.<sup>322</sup>

Having formed earlier than most oil holdings (1991), Lukoil was in a position to offer immediate material benefits: integration into global and international markets and greater access to officials in Moscow. The regional administration played the role of arbiter between national- and regional- level business elites, and brokered an agreement between the Perm financial industrial group and Lukoil, headquartered in Moscow, in

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<sup>320</sup> "Po Standartam Lukoila," *Neft Rossii*, no.4, 2002, 30-33.

<sup>321</sup> Ibid.

<sup>322</sup> Dmitry Gorbuntsov, "Vtoroe Dykhanie Lidera" *Neft Rosii*, No.4. 25-29.



which each side received a 50% interest in Lukoil-Permneft. Lukoil also signed a formal agreement with the regional administration outlining its investment responsibilities. Beyond the agreement, the arrangement with the regional administration was beneficial for Lukoil to the extent that it was able to maintain an “insider” status in the region, effectively gaining a de-facto monopoly position in the region’s fuel markets.<sup>323</sup>

Over two years before the merger was official, Lukoil management in Moscow helped the company develop a financial and strategic marketing plan that would alleviate its colossal debt burden and eliminate redundancies in its management structure, including vertical integration and the consolidation of several smaller enterprises. By March of 1995 cooperation with Lukoil Moscow had begun to bear fruit, as Permneft was able to eliminate wage delays. Likewise, the petrochemical company Permnefteorgsintez, which began negotiations with Lukoil over vertical integration into its national structure in 1991-1992, boasted in 1995 of achieving European and US ecological gasoline standards thanks to the expertise of Lukoil specialists.<sup>324</sup> While there were points of conflict between the regional administration and the Moscow corporate office during the 1990s, such as disputes over the use of pricing techniques (transfer pricing) that reduced tax receipts on oil in the region, the two sides were able to quickly come to terms.<sup>325</sup>

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<sup>323</sup> See N. Lapina and A. Chirikova, *Strategii Regional'nykh Elit, Ekonomika, Modeli Vlasti i Politicheskii Vybor* (Moscow: Russian Academy of Sciences, Institute of Social Sciences, 2000), 110-114, 123-133.

<sup>324</sup> “Po Standartam Lukoila,” 33.

<sup>325</sup> The relationship between LukOil and Perm administration has perhaps been the most cooperative among the national-level businesses in the region. For instance, the Perm administration entered into a protracted conflict with Gazprom for control over an independent gas producer in the region in the late nineties. At the same time, Gazprom and the regional administration also regularly worked together to stimulate diversification in local industry. Lapina and Chirikova, 2000, 89.

Indeed, one reason for Perm's lower level of assertiveness in the 1990s is the cooperative relations established with Lukoil. While the region was called upon to join the Urals Republic proclaimed by governor Rossel in nearby Sverdlovsk *oblast* in 1993-1994, it was already in the process of settling its central jurisdictional issue – control over the oil sector – with Lukoil.<sup>326</sup> And in return for sharing control over the region's most strategic assets (whereas Tatarstan, Bashkortostan, Sverdlovsk and Irkutsk pursued a “winner-take-all” strategy), the administration received various distributional advantages, securing access to external financial resources without the need for the assertiveness displayed by the consistently assertive regions in this arena throughout the 1990s. Finally, the synergy between Lukoil and governor Igumnov in Perm in terms of lobbying federal officials reduced the need for regionalist political mobilization to get Moscow's attention.<sup>327</sup>

The case of Samara is similar to Perm in this regard. Although the region's economy is substantially larger, there have been more national-level actors involved, including the nation's largest automaker, VAZ, Samaraenergo (part of UES), Gazprom and the national-level oil company Yukos. As in Perm, the Samara regional administration adopted a more accommodative strategy in the early part of the transition toward national-level businesses, and supported the transfer of much of the regional oil complex to Yukos.<sup>328</sup> In particular, Samara's oil complex was suffering from the same

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<sup>326</sup> Negotiations with Lukoil were underway in 1993-1994, Gorbuntsov, 25. LukOil-Perm (predecessor to Lukoil-Permneft) was formed as early as 1992. “Po Standartam Lukoila,” 30.

<sup>327</sup> As Peregudov *et al* note, synergy between national-level businesses and regional executives in lobbying (e.g. use of both informal and administrative channels) was highly effective in many regions (pp. 206-207).

<sup>328</sup> See Dimitri Badovski, ‘Samarskaya Oblast v Pervoy Polovine 2000g.’ in *Rossiskiye Regiony-99* (Russia's Regions in 1999), Carnegie Center Moscow, 423.

problems as Perm, in terms of reintegration into the national oil market (e.g. supplies for its oil refineries and markets for distribution) and the need for heavy capital investment. Yukos acquired and integrated smaller regional companies, including Samaraneftegaz and other oil companies in the region.<sup>329</sup> In return for pledges to help revive the region's industry, Titov lobbied for Yukos' interests in the region, helping it to gain an advantage on local markets.<sup>330</sup>

While the consolidation and vertical integration of individual regional oil companies into Yukos was sanctioned by the regional administration, in the beginning the relationship had more rough edges than the Lukoil/Perm arrangement. Yukos began to transfer regional managers to its headquarters in Moscow, replacing them with personnel from outside the region, which forced governor Titov now had to deal with corporate headquarters to solve problems that previously could be addressed with the regional elite.<sup>331</sup>

In addition to the disruption of existing relationships between the regional administration and oil industry in the region, there were also economic problems that arose. Yukos initially had trouble coordinating supplies for regional assets such as Kuibyshevneftorgsintez within its national structure, resulting in lower levels of

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<sup>329</sup> See Yakov Pappé, "Fuel and Energy Complex Elites in the Political Economy of Contemporary Russia," in Klaus Segbers and Stephan De Spiegeleire, eds., *Post-Soviet Puzzles: Mapping the Political Economy of the Former Soviet Union*, (Baden-Baden: Nomos-verlagsgesellschaft, 1995); and Lane, 15-45.

<sup>330</sup> Titov also coordinated relations among the businesses themselves, lobbying VAZ to retain Yukos as its fuel supplier at one point. See Philip Hanson, et al, "Samara and Krasnodar," in Hanson and Bradshaw eds, 2000, 174-181.

<sup>331</sup> For instance, Badovsky notes that leading members of the regional oil elite, such as V. Tarkhov, V. Kazakov and L. Simanovskiy, were transferred to Yukos headquarters in Moscow. As regional elites (e.g. part of the existing *nomenklatura* system prior to Yukos' expansion) were replaced by "outsiders," governor Titov increasingly had to deal with Yukos corporate headquarters in Moscow. Badovskiy, 1999, 423. Perm, by contrast, had less change of regional elite management in the oil sector.

output.<sup>332</sup> In the same vein, the relationship between the regional administration and Yukos initially deteriorated after its acquisition by Bank Menatep in mid-1996, which changed its tax home, denting regional coffers. While this problem was solved by mutual agreement in Perm, the conflict between the region and Menatep over regional revenue forced Titov to appeal to Moscow, and the question of the allocation of revenue between Yukos and the regional administration was addressed in the region's bilateral power-sharing treaty.<sup>333</sup>

Likewise, AvtoVAZ, the nation's largest auto-maker, certainly had sufficient economic clout to lobby its interests at the federal level, while its large share of the region's budget and workforce (esp. in Toliatti) gave it considerable influence within the oblast.<sup>334</sup> For instance, in 1994, VAZ's general director had a seat on the Presidential Council along side national politicians and regional governors. The company also had access to outside financing and markets, mainly through national financiers, such as Boris Berezovsky (LogoVAZ, sales/distribution network and bank). While these channels generally allowed the company to circumvent the regional administration in its rent-seeking activity, Titov's connections with the Prime Minister (via his position on the leadership council of the party of power, Our Home is Russia) and formal power attained through the bilateral treaty allowed him to defend both Yukos and VAZ from the tax

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<sup>332</sup> Pappe, "Fuel and Energy Complex Elites."

<sup>333</sup> IEWS, Russian Regional Report, 6 September, 1997.

<sup>334</sup> VAZ accounts for about a quarter of regional corporate tax revenue, and around 40% of industrial output. Hanson et al, 174-181.

authorities at various times.<sup>335</sup> The result was a more cooperative relationship, while each side maintained their autonomy.

At the same time, the presence of strategically important national-level businesses in a region is a constant source of leverage for the federal center. In November 1996, VAZ was put on a list of companies being prepared for bankruptcy due to arrears owed to the federal budget. This overlapped with negotiations between Samara and the federal government over the region's bilateral power-sharing treaty. In fact, several observers believed that the two events were linked and saw the placement of VAZ on the tax police "black list" as an attempt by the federal government to undermine Titov's bargaining position, due to VAZ's importance for the regional economy. Ultimately, Titov was able to hold his ground; VAZ and the government arrived at agreement on restructuring its federal excise tax.<sup>336</sup>

In general, the cases of Perm and Samara reflect the same type of corporatist-type arrangements between the regional administration and business as in the cases of Irkutsk and Sverdlovsk. However, the presence of national-level businesses in Perm and Samara resulted in "vertical" corporatist arrangements, providing alternate channels to federal level patrons and reducing the need for the degree of reliance on internal resources that motivated assertiveness. The role of national-level businesses as "carrots" was widespread among other loyal regions as well, including Nizhny Novgorod and

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<sup>335</sup> The power-sharing agreement included provisions to restructure tax debt of major enterprises into shares held by the regional administration until the debt was paid off. IEWS, Russian Regional Report, 6 September, 1997.

<sup>336</sup> *Segodnya*, 10 November 1996.

Leningrad *oblast*, where governors also actively depended on national-level business actors for financing state pension payment schemes and capital investment.<sup>337</sup>

One of the key features of the stability of arrangements between national-level businesses and regional political elites in these regions is the relatively even balance of power: both governors have enjoyed their own power bases in regional industries apart from more independent national-level actors. For instance, Titov's power base comes from the region's export-oriented defense (high-tech) sector, which is among the most competitive in Russia. Governor Igumnov in Perm presided over the chemical sector in the region, and (similar to Rossel in Sverdlovsk) set up a corporation that controls virtually all exports of chemical fertilizers in the oblast.<sup>338</sup> In addition, the process of penetration is also important, as in both cases the entrance of national-level businesses was negotiated, based foremost on formal agreements with the regional administration.

### *The Other Side of the Coin: Big Business as a Stick*

While the initial phase of expansion in Samara and Perm was primarily the result of economic necessity and cooperation among national-level businesses and the regional administration, others instances of expansion by Moscow-based banks tended to be more conflictual. For instance, not all oil-rich ethnic republics were as successful as Tatarstan and Bashkortostan in keeping control over their resources and strategic assets largely in

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<sup>337</sup> See Andrey Chugunov, "Neft Ukhodit na Pensiyu," *Kommersant*, no.6, 18 February 1997; "Gubernatory Delayut Den'gi," *Kommersant*, no.43, 19 November 1996, 19. In the case of Nizhny Novgorod, the oil companies Yukos and Lukoil helped to finance the region's pension system after the federal center continuously delayed payments starting in August 1995 and initial threats against the federal authorities fell on deaf ears. Likewise, as soon as he was elected governor of Leningrad Oblast, L. Gorbenko appointed a team of deputies to solicit funds from Moscow-based big businesses operating in the region for financing construction projects.

<sup>338</sup> Lapina and Chirikova, 2000, 109-114.

the hands of the local *nomenklatura*. Despite resistance from local elites, the republic of Udmurtia saw the majority of its oil assets (wells and refineries) integrated into the Sidanko holding, a national-level oil company which came under the control of the Oneksim group.

Having gained a foothold in the region, in 1996-1997 Oneksimbank was able to use its financial clout to expand its control over key assets in the republic's oil complex and financial infrastructure. For instance, the bank leveraged an agreement with the republic administration whereby it extended a loan for 100 billion rubles (prior to currency redenomination) in return for the right not only to service regional budgetary flows, but also to take control of the bank servicing the regional budget, and to receive a stake in the republic's main oil product distribution company.<sup>339</sup> Local observers saw Oneksim's "takeover" of the region's fiscal system as a threat to the region's economic and political autonomy.<sup>340</sup> The same type of pattern took place in other regions; in Yaroslavl, Oneksim paid off a 1 trillion ruble debt of the administration to commercial banks and the federal budget in exchange for control over regional fiscal flows and the servicing of federal programs, despite the dubious legality of the measure.<sup>341</sup>

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<sup>339</sup> Sidanko controlled about 70% of oil extraction in the republic by 1997. The bank received a stake in "Udmurtnefteprodukt," the republic's sales and distribution network of oil products. "Bank s Gosudarstvennym Myshleniem Stroit Sobstvennoe Gosudarstvo," *Finansovye Izvestiya*, 11 February 1998.

<sup>340</sup> The "takeover" of a region could also extend to the political sphere as well as financial. In Tyumen, for instance, gubernatorial elections came to be dominated by shifting coalitions of national-level companies in competition with one another.

<sup>341</sup> Ibid. For instance, Oneksim bank's capital in 1996 was more than three times the entire regional budget, and it extended a 1 trillion ruble loan to the *oblast*. Having taking over servicing of the regional budget, the bank also gained political influence in the region since the majority of regional enterprises depended on the regional budget for support. It also took over the servicing of federal programs, mainly through its personal contacts in MinFin.

Likewise, the struggle over Norilsk Nickel in Krasnoyarsk is an example of how the change in ownership of national-level manufacturing enterprises could engender a shift from cooperative to conflictual relations between the regional administration and national-level business. Upon acquisition of a stake in Norilsk Nickel in late 1996, Oneksimbank entered into a struggle with its CEO, Anatloy Filatov, for effective control over the company, which was heavily in debt to RAO UES, and also to its workers. The bank was able to gain the workers on its side by purposely exacerbating the wage arrear problem.<sup>342</sup> Of particular interest is the synergy between Oneksim and the federal government, in terms of the increased scrutiny Filatov came under: Norilsk was visited by a plethora of government commissions, from the prosecutor's office, tax police, special government commission – and even a foreign auditor. Despite appeals to PM Chernomyrdin and President Yeltsin, Filatov was eventually forced to resign by the trade union. The bank then “found” 10 billion rubles in financing and debt-relief in Moscow to address the company's indebtedness and pay the workers.

The change in management immediately impacted the regional budget of Krasnoyarsk, due to reduced tax payments from lowered profits attributed to the enterprise's local operations, which contribute a significant share of the regional budget.<sup>343</sup> In the beginning of 1997, Governor Zubov appealed to the federal government to have Oneksimbank stripped of its Norilsk Nickel shares and to have them placed under the control of regional officials. Despite the governor's continued pleas, Onesksim won a

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<sup>342</sup> Natalya Gotova, “Anatoly Filatov Steps Down After All,” *Sevodnya*, April 16, 1, *Current Digest of the Soviet Press*, Vol 48, No 16 (1996), 9; “Why Did the Nickel King Step Down?” *Izvestiya*, April 16, 2.

<sup>343</sup> Alexsei Tarasov, “Filatov, the Nickel King, Steps Down,” *Izvestiya*, February 23, 2; *Current Digest of the Soviet Press*, 48 No 8 (1996).



contested privatization tender later in 1997 awarding it a controlling stake in the company – thanks largely to its patrons in the federal government.<sup>344</sup>

In less cooperative forms of expansion, big business' entry into a region was accompanied by the virtual takeover of the region's fiscal infrastructure, as in the case of Udmurtia, or a protracted conflict between national-level businesses and regional political elites, as in the case of Krasnoyarsk. In both cases, however, the end result was lesser degrees of assertiveness. In effect, Oneksim bank was the intermediary between the federal budget (as an authorized bank which received the right to service federal funds) and Udmurtia's budget; as such, it offered the republic an alternate channel for solving the region's fiscal problems other than direct assertiveness. Likewise, Krasnoyarsk authorities sought the support of the federal center in their struggle with Oneksimbank, which raises the costs of assertiveness toward Moscow.

These instances provide contrast to the relatively smooth process of national-level consolidation in Samara and Perm. In general the "imperialistic" form of expansion was generally unstable: while it forced loyalty for some periods, shifts in the balance of power and flare-ups of resentment of being "taken over" by "Moscow-based" elites – an increasingly common electoral theme by the end of the 1990s – set the stage for further assertiveness, including a "tax revolt" by Governor Lebed, and support of pro-region parties in the late 1990s.<sup>345</sup> Moreover, both Udmurtia and Krasnoyarsk would eventually hold out beyond the July 2002 deadline for treaty abrogation.

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<sup>344</sup> Ibid.

<sup>345</sup> "Kremlin Succumbs to Blackmail," *Current Digest of the Soviet Press*, Vol 50; No.18 (1998), 14. Krasnoyarsk was apparently more successful in coercing the government to pay of a 50mln ruble debt in

## SECOND WAVE OF EXPANSION UNDER PUTIN

The months immediately following the August 1998 financial crisis provided a strong impulse for regional autarky: political uncertainty and the paralysis of the fiscal system weakened both the federal center's political will and its ability to effectively police the national market. Assertive and loyal regions alike attempted to expand their control over economic activity within their jurisdictions, and perhaps "grab back" strategic assets on their territories, as the financial arms of national-level businesses collapsed or were forced to divest assets. At the same time, the window of opportunity proved to be rather narrow, and none of the national-level businesses were broken up and taken over by regional elites.<sup>346</sup>

On the contrary, in 1999 a resurgent united federal center began to encroach upon both the fiscal resources and policy authority of regional governments, especially in the regulatory and law enforcement spheres. Concurrent with the mounting pressure for political and fiscal recentralization, a second wave of national-level expansion and consolidation began, especially in the metals sector. Empowered by the positive effects of devaluation on relative prices, national-level actors began to transform themselves into more tightly integrated business groups formed around flagship industrial assets instead of "authorized banks," as was the case previously.<sup>347</sup>

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May, 1998, as leaders also threatened to hold a referendum on the region's political/legal status in the Federation.

<sup>346</sup> See Sledzevsky, I.V., "Regionalism in the Russian Federation as a New Sociocultural Reality" in *Federalism and Regional Relations* (Moscow: Ethnosphere, 1999).

<sup>347</sup> Yakov Pappé, "Krupniy Biznes v Rossiskou Ekonomike," paper delivered to the Russian Academy of Sciences (Nauchniy Soviet, INP/RAN) 30 May, 2001; S. Avdasheva and V. Dement'ev, *Analiz Roli Integrirovannykh Struktur na Rossiyskikh Tovarnykh Rynkakh* (Moscow: Tezis, 2000).

The Kremlin's attempt to strengthen central state autonomy from a narrow group of insiders that emerged in the mid- to late 1990s, evened the playing field for national-level businesses competing for choice regional assets. A meeting between President Putin and the business "oligarchy" in summer 2001 resulted in an informal pact affirming the principal of non-interference: the Kremlin would remain aloof from business, while business would stay out of politics.<sup>348</sup> Some regional observers equated the second wave of expansion with the construction of an "economic vertical of power" complimenting the construction of Putin's political hierarchy embodied in the institution of the federal district system.<sup>349</sup>

An important aspect of the second wave of national-business expansion from 1999-2002 is that the 1998 crisis and decline of the role of Moscow-based "authorized banks" served to align the interests of national-level business elites with regional politicians to a greater degree, since the "real economy" (rather than financial arbitrage, contorted intra-group asset-transfers and tax-evasion schemes) became the bread and butter of national-level business groups.<sup>350</sup> Asset stripping has been largely replaced by capital investment in regional factories; while capital flight remains a major problem, domestic investment on the part of big business groups has increased sharply.<sup>351</sup> Thus,

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<sup>348</sup> See for instance, A Mukhin, *Novie Pravila Igry Dlya Bol'shogo Biznesa, Prodiktivannye Logikoy Upravleniya V.V. Putina* (Moscow: Gnom&D Publishers, 2002).

<sup>349</sup> Excerpt from article in *Vecherniy Chelyabinsk* quoted by *Intersvyaz* News Agency, December 21, 2001. Yuliy Gorbunostov, "Vertikal Vlasti i Territorial'nye Zagoguliny," *Nezavisimaya Gazeta*, January 28, 2002.

<sup>350</sup> Interview with Elena Romanova, economist at Raiffeisenbank Moscow, April 17, 2001.

<sup>351</sup> *Ibid.*

after 1998, there was more common ground for cooperation between regional political and national business elites.<sup>352</sup>

At the same time, under Putin national-level businesses are more often being used a “stick, ” especially in terms of effecting a change in leadership in a particular region, rather than merely a carrot as in the 1990s (e.g. corporatist arrangements which might not necessarily benefit the federal center). Some of the examples below indicate this trend of increasing synergy between the national-level businesses and the Kremlin in influencing electoral outcomes at the regional level.<sup>353</sup>

### **Second Wave of Penetration: Divergence of Irkutsk and Sverdlovsk**

The stories of Irkutsk and Sverdlovsk had similar beginnings, as executives in both regions were able to protect strategic sectors of their economies from integration into national-level businesses during the first wave of expansion. However, during the second wave, Irkutsk’s enterprises increasingly became the targets of acquisition. From 1999-2002, a handful of large metal and machine-building holdings emerged, including RusAl and Sibal, which account for over 70% of national aluminum production, as well as SuAl, controlled by Alfa Group. In particular, RusAl meets the criteria for a national-level business according to both size and structure (see Table 4.1, second to the last row). An important consequence of the emphasis on vertical integration in this sector has been the increased interest of national-level business elites in regional electricity generating

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<sup>352</sup> Andrey Serenko, *Novaya Regional’naya Politika: Financovo-promyshlennye Gruppy Menyayut Priority*, report published for the Center for Political Technology (politcom.ru), 2000.

<sup>353</sup> See Zubarevich, 2002.

stations (aluminum production is electricity-intensive) and automobile factories.<sup>354</sup> Also, national business groups began to expand in the coal sector, which is a major fuel supplier to the electricity sector and an alternative to natural gas, the supply of which is largely controlled by the Gazprom monopoly.

During the second wave of expansion, several key regional-level manufacturing enterprises in Irkutsk were integrated into national-level business groups, including the Bratsk Aluminum Plant (RusAl) and Irkutsk Aluminum Plant (Sual/Alfa Group). The redistribution of control over the region's strategic assets also led to a dispersal of power within the region, continuing the process already begun by the incorporation of the Angarsk refinery into Sidanko (Oneksimbank) mentioned above. In particular, the region's key economic asset, Irkutskenergo, became a target of rivalry between the national-level businesses operating in the region, as did its coal, gas and gold fields. Unable to completely fend off national-level expansion, Irkutsk governor Govorin instead chose a strategy of selective co-optation in order to preserve the influence of the regional administration as broker in the power struggle between national-level actors in the region. Ahead of the 2001 gubernatorial elections in the region, Govorin forged an alliance with RusAl and Alfa to counter Oneksimbank, which was supporting a challenger in the gubernatorial campaign. In exchange, Govorin used his voting packet to appoint a general director at Irkutskenergo who was supported by Rusal and Alfa.<sup>355</sup>

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<sup>354</sup> Interview with Nikolai Lukashenko, Raifeissenbank Moscow, May 2002.

<sup>355</sup> Turovskiy, "Kontekst Vlasti: Gubernatory i Oligarkhi: Istoriya Otnoshenie," report published for the Center for Political Technology (politcom.ru), 2002.

Sverdlovsk *oblast* was also affected by the second wave of national-level expansion on the heels of the financial crisis. Governor Rossel participated in the creation of joint gas, oil and steel companies with various national-level businesses.<sup>356</sup> Compared to Irkutsk, however, Sverdlovsk has a much wider base of large regional-level enterprises, many of which were part of the bloated Soviet defense sector. In addition, Sverdlovsk is in the minority of wealthy regions demonstrating executive elite continuity from the Soviet period. Although Rossel by no means has a monopoly on political activity in the region, he still enjoys a well-established administrative power base and steady support from local industrialists.<sup>357</sup>

Thus, after the second wave of expansion, the political influence of national-level businesses in the region was limited enough that Rossel was able to maintain an assertive strategy (unlike Irkutsk, Sverdlovsk was among the “problem regions” cited in Table 5.2) without having to fear that the use of national-level businesses as “sticks” would be enough to unseat him. The Kremlin did try, however. There was a half-hearted attempt by the Kremlin-supported party of power, United Russia, to establish Sergey Nosov, director of the local metals giant Nizhny Tagil (part of Evrazholding, which emerged as a national-level business in 2001) as a viable competitor to Rossel in the gubernatorial elections.<sup>358</sup> However, the unexpected success of *Za Rodnoy Ural*, Rossel’s party which enjoys a strong base of support in regional-level industry, in local legislative elections

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<sup>356</sup> Yaroslav Startsev, “Gubernatorial Politics in Sverdlovsk Oblast,” *Post-Soviet Affairs*, 15, 4, (1999): 336-361.

<sup>357</sup> Peregudov et al, 191.

<sup>358</sup> Nizhny Tagil was integrated into Evrazholding, which entered the top echelon of enterprises in 2001 (see Table 4.1).

doused United Russia's hopes of unseating Rossel in the gubernatorial race, simultaneously lowering the Kremlin's political leverage over the governor.<sup>359</sup>

Although all the formerly assertive regions were affected by the second wave of expansion, a bifurcation began to take place. Sverdlovsk's industrial base has been sufficiently large and diversified to absorb national-level expansion without undermining Rossel's power base.<sup>360</sup> Irkutsk's political economy, on the other hand, is made up of a substantially narrower group of enterprises. With the rise of national-level business influence in the oblast, especially over the management of Irkutskenergo, the regional administration was forced to switch to a strategy of sharing effective control over major regional assets – and, respectively, influence over the regional economy – with national business elites. The value of the power-sharing agreement as a tool to protect the region's chief assets from outside control had proved to be rather limited. In addition to RusAl's greater influence over Irkutskenergo, the Angarsk refinery, Bratsky aluminum and Irkutsk aluminum enterprises were also integrated into national-level businesses, accounting for the bulk of the region's strategic assets.<sup>361</sup>

For the sake of comparison, two ethnic republics with higher levels of assertiveness in the 1990s, Komi and Yakutia, will be briefly mentioned. Komi's largest oil company, KomiTek (which was an autonomous republic company similar to Bashneft and Tatneft), was taken over by Lukoil in 1999. The takeover of KomiTek was accompanied by an electoral defeat for the incumbent governor, Yurii Spiridonov, who

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<sup>359</sup> Vitaly Sotnik, "Za Rodnoy Ural, za Gubernatora Rosselya," *Nezavisimiaya Gazeta*, April 23, 2002.

<sup>360</sup> For instance, Nizhny Tagil has accounted for less than ten percent of Sverdlovsk's industrial output over the period.

<sup>361</sup> Bradshaw et al, 2000, 205.

had opposed Lukoil's expansion into the region.<sup>362</sup> The change in leadership and subsequent rise of national-level business influence in the region's political economy also had an impact on its level of assertiveness: among the wealthy republics, Komi was the only one to comply with the July 2002 deadline for abrogation of power-sharing agreements.<sup>363</sup>

In a similar vein, the republic of Yakutia also underwent a change in leadership with the participation of a national-level business. The republic is highly dependent on Russia's largest diamond company, AlRosa, for a significant portion of its revenues. In a scenario similar to the ousting of Filatov from Norilsk Nickel in the 1990s, as part of its drive to unseat incumbent President Mikhail Nikolyaev, the Kremlin activated the Audit Chamber and other federal organs to pressure the company, securing the loyalty of Vyacheslav Shtyrov, general director of the company.<sup>364</sup> Nikolyaev ultimately conceded to the Kremlin's pressure and Shtyrov became president of the republic. Although Yakutia held out beyond the deadline for abrogation of the power-sharing treaties, it was not included in the list of problem regions (as were the republics Bashkortostan and Tatarstan, for instance). Moreover, in a sign that the leadership change bore fruit for the Kremlin in terms of overcoming regional defiance, the republic complied with the federal law and re-negotiated its treaty not long after the deadline, in November 2002.<sup>365</sup>

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<sup>362</sup> Yurii Shabaev, "Business Dominates Komi Politics" *Russian Regional Report* (Vol. 8, No. 4, 14 March 2003). To add insult to injury, in March 2003 elections to the regional legislature, Lukoil-Komi General Director Vladimir Mulyak defeated former President Spirindonov.

<sup>363</sup> *Rossiiskaya Gazeta* legal database.

<sup>364</sup> RFE/RL Russian Federation Report, 30 January 2002, Vol.4, No. 3

<sup>365</sup> *Rossiiskaya Gazeta* legal database.



## Deepening Penetration: Loyal Regions

The loyal regions generally witnessed a deepening of national-level penetration during the 1999-2002 period, marked by continuity in the “vertical” corporatist arrangements established in the early to mid-nineties. Regions that had already adopted a power-sharing strategy with national-level business were less assertive of their individual autonomy in this period. Both Perm and Samara complied with the Kremlin’s campaign to phase out the power-sharing arrangements by the July 2002 deadline, while Governor Yuri Trutnev in Perm was one of the first to publicly support the annulment of the treaties.<sup>366</sup>

The parliamentary elections in 1999 and ensuing wave of gubernatorial elections in 2000-2001 highlighted the continued influence of national-level businesses in these regions. Since 1995, the leaders of both regions supported the federal government’s party of power, *Our Home is Russia*, which had effectively disintegrated after its leader, V. Chernomyrdin was rejected as Prime Minister by the Duma in fall 1998. During the 1999 parliamentary election campaign, Samara governor Titov joined the SPS party (Union of Right Forces), a pro-Kremlin party that received financial and political support from Anatoly Chubais, head of the United Energy Systems, one of the largest national-level business structures.<sup>367</sup>

In Perm governor Igumnov identified with the All Russia party, which was pitted against the Kremlin’s party of power, Unity. Initially, Igumnov’s identification with the

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<sup>366</sup> “Dlya Nashey Oblasti Privilegii net,” *Noviy Kompan’on*, No.24 (177), 1. See chapter 3 of the dissertation for a more detailed discussion of these region’s reactions to the federal mandate.

<sup>367</sup> Samaraenergo (part of UES) is also an influential national-level business in Samara.

party reflected the specific influence of national-level business on the political orientation of regional executives. Lukoil headquarters in Moscow participated in the creation of All Russia, in hopes of creating a successor party to NDR (Our Home is Russia), the “party of power” since 1995 parliamentary elections.<sup>368</sup> Following the lead of its head office, Lukoil-Perm also threw its support behind the party. However, Lukoil Moscow eventually cooled off towards “All Russia” as it became more regionalist in orientation, especially after it merged with Luzhkov’s “Fatherland” party. Indeed, the party’s main base of support in the outgoing Duma, the “Russian Regions” faction led by Oleg Morozov, issued a statement to its regional cells that they could also solicit votes for the Unity party, already anticipating the strategic alliance between the two that was to take place on the eve of presidential elections in March 2000.<sup>369</sup> The difference between Lukoil’s position (mirrored by Oleg Morozov/Russia Regions faction) and the regional leaders on the leadership council (Tatarstan’s Shamiev, for instance) is that the former were much less concerned with defending the asymmetrical federal system and more concerned with being on the “winning” side, favoring corporatist over programmatic goals. Thus compared to the assertive regions in the first category, Perm’s support for pro-regionalist parties was considerably less enthusiastic. Unlike Igumnov, the leaders of Tatarstan, Bashkortostan and Irkutsk were on the leadership council, while Rossel presided over his own home-grown party, *Za Rodnoy Ural*.

Subfederal elections also reflected the deepening influence of national-level businesses. By 2000, many of the rough edges of the relationship between Yukos and

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<sup>368</sup> Lapina and Chirikova, 2000, 154-172.

<sup>369</sup> Ivan Rodin, “Vremya Rykhlykk Soyuzov Minovalo,” *Nezavisimaya Gazeta*, October 10, 2001, 2.

Samara had been smoothed over, in part due to changes in Menatep group's management style and its commitment to investment and growth in its strategic regions.<sup>370</sup> Another motivation for a tighter alliance was the 2000 gubernatorial race, when Yukos emerged as a key supporter of Titov, whose grip on power was initially challenged by another national-level business in the region, Gazprom, which had forwarded the candidacy of one of its former executives.<sup>371</sup> Upon Governor Titov's re-election, he cemented his relationship with Yukos via an "exchange of cadres." Yukos executive vice president, V. Kazakov, who headed up Titov's campaign headquarters, was appointed deputy governor of Samara, while Titov's son was given a position in a Yukos-related bank.<sup>372</sup>

In Perm, Lukoil-Perm modestly supported governor Igumnov's reelection bid, although the company had to temper its enthusiasm due to considerations of its federal-level ties. The presidential representative for the Volga region, Sergey Kirienko, was trying to engineer Igumnov's defeat in the elections to Yuri Trutnev, the mayor of the city of Perm.<sup>373</sup> Trutnev defeated Igumnov in the election, and the new governor and Lukoil quickly found common ground and signed a new cooperation agreement in 2001. The agreement included a five-year plan allotting financing to develop various social projects in the *oblast*, in the spheres of education and training, infrastructure, housing,

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<sup>370</sup> Badovsky notes that in the late 1990s Yukos also began to rotate managers back to Samara that had earlier been transferred to Moscow (V. Tarkhov, V. Kazakov). Badovskiy, 420-423. See also Serenko, 2001 for general changes in strategic management of transregional financial-industrial groups after the 2000 elections. Chapter 6 deals with the issue of corporate social responsibility, which ranked higher on Yukos' agenda after 2000, to a large degree due to Khodorkovsky's own political ambitions.

<sup>371</sup> Ibid.

<sup>372</sup> Turovskiy, 2002, 3.

<sup>373</sup> Center for Political Information, "Volga Federal District," 2002, 8-12. Apparently, Lukoil helped Trutnev during the campaign as well, instead of putting all of its eggs in one basket.

etc.<sup>374</sup> After signing the agreement, Trutnev acknowledged that relations between Lukoil and the regional administration remained the most important for the region.<sup>375</sup> At the same time, Lukoil provided former governor Igumnov with a golden parachute: the outgoing governor went to work for Lukoil-Permneft at the end of his term.<sup>376</sup>

The cases of Perm and Samara in 1999-2002 represent continuity in cooperative arrangements between national-level business actors and regional political elites, together with exchanges of cadres between the executive branch and businesses. Having current or former managers in the regional administration was obviously beneficial for national-level business, in terms of influencing regulatory and administrative decisions, especially given the dominance of the executive branch in the Russian polity.<sup>377</sup> Likewise, alliances with national-level businesses have extended beyond electoral support, to include support for family members and golden parachutes. Such patterns of exchange have helped to cement relations between big businesses and regional administrations in other loyal regions as well.<sup>378</sup> In the case of Perm, the relative ease at which Lukoil entered into an alliance with the new governor reflects the fact that cooperative-type penetration is predicated on more than just personal relations in the consistently loyal regions.<sup>379</sup>

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<sup>374</sup> “U Vlasti i Biznes Zaboty Obshchie” *Neft Rossii*, No.4, 2002, 34-35.

<sup>375</sup> Ibid. Trutnev remarked that LukOil-Permneft accounts for around a third of the regional budget.

<sup>376</sup> Turovskiy, 2002, 5.

<sup>377</sup> Barany and Moser, 2001.

<sup>378</sup> For instance, a similar pattern took place in Nizhny Novgorod, where Lukoil had supported the incumbent Sklyarov, who lost, only to strike a deal with the winner, Khodyrev. One of the results was the selection of the new *oblast* minister of finance (V.Sobolev) from a LukOil controlled bank. Turovskiy, 2002, 4-5.

<sup>379</sup> According to Turovsky, (pp. 3-7) similar example of these “exchanges of cadres” have taken place in other regions where national-level businesses are influential, such as Omsk (where the son of governor Pozhelaev was given a position in a company owned by Roman Abramovich) and Nizhny Novgorod (where the son-in-law of governor Sklyarov was given a position in Lukoil).

## CONCLUSION

This chapter has presented a framework for categorizing the wealthy regions based on the timing and nature of national-level business expansion. Within the context of Chapter 3, which charted out the dynamics of regional assertiveness across the three phases of intergovernmental relations from 1990-2002, three categories can be identified. Two of the categories, consistently assertive and consistently loyal, emphasize continuity. Regions in the first category have repeatedly asserted their jurisdictional rights to protect strategic sectors of the economy from penetration by national-level businesses in the face of shifting federal strategies over time. These regions were the boldest seekers of autonomy in the early 1990s when Yeltsin implored the regions to “take as much sovereignty as you can swallow;” they pushed for the best deals during the period of selective accommodation (e.g. asymmetrical federalism) in the mid to late 1990s; and have most vigorously resisted the harmonization of regional rights and abrogation of the power-sharing treaties under Putin. Likewise, the heavy amount of financial resources needed to protect strategic regional enterprises from being taken over by national-level businesses has dictated continued assertion in the distributional arena. Sverdlovsk, for instance, was one of the most vocal regions in terms of fiscal and economic protests in support of local industries in the 1990s.

Likewise, there has been a deepening, or gradual institutionalization, of the relationship between national-level businesses and regional administrations in those consistently loyal regions such as Perm and Samara. The cooperative relationship

between Lukoil and the Perm regional administration has survived changes in regional leadership, suggesting that it has evolved beyond merely personal connections. The “carrots” offered by national-level businesses to regional enterprises in Perm and Samara have included integration into broader markets and greater sources of financing and technical expertise. Moreover, national-level businesses have played a major role in financing regional development programs, as in Perm. In the case of Samara, many of the initial rough edges between Yukos and the administration following its acquisition by Menatep were smoothed over with an electoral alliance and solidified by an exchange of cadres. Both regions have demonstrated lower levels of assertion under Yeltsin, and were among the first to abrogate their bilateral power-sharing treaties under Putin.

While the first two categories emphasize continuity on either side of the spectrum, the third category highlights a pattern of change. As the independent variable in this study – the degree of penetration of national-level business – has increased, the dependent variable, regional assertiveness, has decreased. As national-level businesses have expanded into Irkutsk, for example, the opportunities for the regional administration to pursue a “winner-take-all” strategy have diminished, while federal elites’ political leverage has grown. As the region became increasingly overrun by national level businesses, such as RusAl, Alfa, Oneksim, Yukos, etc., the formal value of the region’s power-sharing treaty as a tool to protect strategic regional assets ultimately proved to be ineffective, which may be one reason why the region was less publicly defiant (relative to Sverdlovsk, for instance) in the face of the Kremlin’s campaign to phase out these treaties. Finally, among the ethnic republics with increasing levels of penetration,

national-level businesses have also served federal interests in both Yakutia and Komi, by acting as a counterweight to the administrative resources of incumbents, both of whom were replaced. Accordingly, all of these regions saw declining assertiveness from the Yeltsin to the Putin period relative to regions in the first category.

## **Chapter 6: Conclusion**

This dissertation ultimately centers on a puzzle. In the comparative literature, natural resource wealth and industrial development have traditionally been associated with higher levels of assertive behavior by regional governments in federal systems, such as demands for state restructuring and expansion of control over fiscal and political resources. Yet, empirical observations of regional behavior across both the Yeltsin and Putin presidencies reveal a seemingly inexplicable divergence among similarly endowed regions. While some wealthy regions have consistently pursued assertive autonomy-seeking strategies, others have demonstrated much more restraint and “loyalty” toward the center. The traditional drivers of regional behavior found in the Russian area literature cannot explain this puzzle adequately. While the Soviet Union’s ethnofederal legacy does explain part of the variation, it cannot account for the divergence of behavior within the subsets of equally wealthy “ethnic” republics and “Russian” regions. Moreover, this divergent pattern has remained consistent across time despite the redesign of federal institutions and changes in national leadership. Solving the puzzle has important implications not only for Russia’s political future, but also for our understanding of the role of federalism in transitional regimes.

This study is intended to fill in the gap in the literature. My central argument is that unexpected patterns of restraint and cooperation can be explained by the role of a “third player” in the federal bargaining game: national-level businesses. Due to its size and structure, the top echelon of businesses in Russia influences both economic



incentives and political opportunities for regional assertiveness. National-level businesses' primary dependence on federal politicians to operate successfully in national and international markets, coupled with their aversion to various forms of regional (e.g. sub-federal) protectionism and economic populism, make them natural allies of the federal center. In regions where they have strategic interests, national-level businesses have used their political influence and financial resources as both "carrots" and "sticks" to mediate intergovernmental conflict and deter potentially disruptive behavior by regional politicians.

Both quantitative and qualitative modes of analysis support the thesis that national-level business actors have helped structure federal relations in Russia. The multivariate regression controls for customary explanations of assertive regionalism, and finds that the relative amount of resources controlled by national-level businesses in a region is negatively correlated with its assertiveness from 1990-2002. The higher the concentration of national-level business actors in a region, the lower that region's level of assertive behavior. This effect has been strongest following the "first wave" of national business expansion that took place in the first half of the 1990s, when the energy sector was consolidated and carved up into vertically-integrated companies, most of which have been based in Moscow.

Moreover, controlling for the wider set of large regional enterprises in the model reinforces the dissertation's thesis that the relative size of business actors affects their ability to integrate, rather than fragment, the federal state. Consistent with the conventional wisdom, heavier concentrations of regional industries were positively

correlated with assertive regional behavior in the regressions. However, when the subset of national-level businesses is tested separately, the sign changes from positive to negative. As “shared resources,” national-level businesses have helped restrain intergovernmental competition in the Russian Federation.

A more in-depth look at four Russian regions – Sverdlovsk, Irkutsk, Samara and Perm – suggests that the wealthy regions can be placed into three general categories. Two could be seen as being on the opposite end of a spectrum: consistently “assertive” and consistently “loyal” regions. For instance, the regional administration in Sverdlovsk has been relatively successful in limiting (or participating in) the penetration of national-level businesses in strategic sectors of the region’s economy, which has allowed it to more consistently pursue assertive strategies in the intergovernmental bargaining game. In regions where national-level businesses have maintained a strategic presence since the early part of the transition, such as Perm and Samara, pressing jurisdictional and distributional issues were generally resolved via power-sharing settlements between these businesses and the regional administrations, in place of more risky strategies of assertion toward Moscow.

The third category encompasses regions in the middle of the spectrum that have demonstrated a change in behavior over time. The case of Irkutsk reflects a trend toward declining assertiveness associated with the “second wave” of national-level business expansion into the periphery that has taken place in the metals and machine-building sectors since 2000. As national-level businesses have expanded into Irkutsk, regional elites have been increasingly forced to “share” control over the region’s most strategic

assets. This has altered the political balance of power in the region, reducing incentives for the regional administration to pursue a defiant, “winner-take-all” strategy toward Moscow. As the influence of national-level businesses has grown in the periphery under Putin, so too have the number of regions that have gravitated toward the “loyal” end of the spectrum.

The empirical findings suggest that models of elite bargaining in developing federal systems more fully explain patterns of regional behavior when the political role of big business is taken into account. In the Russian case, a higher concentration of national-level businesses in a particular region has been associated with lower levels of assertiveness. Incorporating the political constraints placed by national-level businesses on regional executives helps to explain the dichotomous pattern among Russia’s wealthier regions. Based solely on macro-structural variables, such as levels of industrial output, export capacity, and natural resource endowments, all the wealthy regions, both ethnic and non-ethnic, have had strong incentives for assertion and high levels of bargaining power.

Likewise, focusing on formal state structures and political institutions alone does not capture the full range of variation in federal outcomes across regions. Non-state actors have mattered in the development of Russia’s federal system. Various federal strategies employing carrots and sticks – such as selective accommodation under Yeltsin and the strengthening of executive vertical accountability under Putin – have also been supplemented with changes in regional politicians’ constituencies as national-level businesses have expanded into the periphery.

The capacity of big businesses to act as mechanisms of political integration reflects a different side of state-business relations than the customary view found in the literature on the Yeltsin era. While big businesses certainly have had a “horizontally” fragmenting effect on government at the federal level by dividing the loyalties of government officials among competing financial-industrial groups, they have also played a “vertically” integrating role. The vertical integration of key sectors of Russia’s economy, such as oil and gas, and more recently, metals and machine-building, has facilitated the construction of economic hierarchies binding the Russian federal state alongside political ones.

Understanding the dynamics of the triangular relationship between the central government, sub-national governments and business actors in federal systems is also important for the comparative study of federal systems. Globalization has increased the influence of big businesses vis-à-vis both national and regional governments.<sup>380</sup> By presenting a theoretical framework that differentiates between the size and structure of business actors and the likelihood of alliances with various levels of government, this study lays the groundwork for further research on the effect of state-business relations on patterns of governance in multi-tiered states.

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<sup>380</sup> Richard Deeg, “Economic Globalization and the Shifting Boundaries of German Federalism,” *Publius: The Journal of Federalism*, 26:1 (Winter 1996), 27-52.

## **IMPLICATIONS: BIG BUSINESS AND THE "FEDERAL BALANCE"**

### **Federalism and Democratic Governance**

I argue that national-level businesses have served as vertically-integrating mechanisms in Russia's federal system, explaining unexpected restraint among the wealthy regions in the context of under-institutionalization of federal institutions and weak national party penetration in the periphery. The first concern that follows from this assertion is whether this is a desirable outcome for the consolidation of Russian democracy. Is regional assertiveness – in the form of demands for greater decentralization and resistance to recentralization – necessarily a thing to be avoided? Secondly, should big business play a political role as an integrating mechanism in Russia's federal system?

In and of itself, the assertion of jurisdictional and distributional claims against the federal center by regional governments, accompanied by various forms of regionalist political mobilization, is not necessarily detrimental for democratization.<sup>381</sup> Democratization and market reform have gone hand in hand with decentralization in many areas of the world, such as Latin America, Africa and Europe. In states with culturally heterogeneous populations and geographically diverse territories, the decentralization of political authority and fiscal resources can promote consensus building and the accommodation of diverse interests in society (e.g. pluralism); increase democratic accountability and policy innovation at the local level; and enhance the ability

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<sup>381</sup> Larry Diamond, *Developing Democracy: Towards Consolidation* (Baltimore: John Hopkins University Press, 1999).

of regional governments to more readily adapt to the fluid opportunities and competitive pressures resulting from market reform and global economic integration.

However, the divergent experiences of various transitional states over the last decade have shown that decentralization can be a double-edged sword. In the absence of sufficiently strong political coordination from above, federal systems can ultimately erode democratic accountability, worsen public sector performance and exacerbate distributional tensions, setting the stage for ethnic conflicts, and political and macroeconomic instability. The literature on the third wave of democratization reviewed earlier singles out federal systems as institutional arrangements that can exacerbate these “dangers of decentralization” due to the perverse incentives and resource mobilization opportunities that they create for regional politicians to assert their geographically particular interests.<sup>382</sup>

Inasmuch as federalism is a doctrine of balance, the central issue for transitional states is finding a middle ground between intergovernmental competition and cooperation that ensures political stability and a unified national legal and market space while constraining the federal center from routinely encroaching on regional competencies, which could undermine incentives for policy innovation and efficiency-enhancing interregional competition. During the 1990s, Russia's federal system was decidedly out of balance. The federal state was plagued by partisan conflict, resulting in weak political hierarchies and excessive, ad-hoc accommodations of regional demands.<sup>383</sup>

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<sup>382</sup> For instance, see Prude'homme, 1995.

<sup>383</sup> Solnick, 1999; Stoner-Weiss, 1999.

Within this context, regional assertion posed a real threat to the central state's ability to manage both the political and market transition. In essence, the penetration of national-level businesses into the periphery has helped to substitute for weak political hierarchies, by deterring regional assertiveness in the public political arena and structuring more cooperative federal relations. At the same time, it is well understood that the magnification of the political influence of big business actors (e.g. Russia's system of "oligarchic capitalism") has also had deleterious effects on formal state capacity at various levels of government. In particular, the political influence of Russia's business oligarchs has been blamed for slowing Russia's market transition.<sup>384</sup>

As stated earlier, Putin has addressed this problem via administrative, legislative and constitutional reforms, such as expanding the authority of the federal district bureaucracy, revamping the Federation Council, the tweaking of Russia's fiscal federal system, abrogation of the bilateral power-sharing treaties and clarification of the rights and responsibilities of federal, regional and local governments (e.g. Kozak Commission legislation) by parliament. These actions could further restore the "federal balance" by enhancing the federal center's capacity to govern more effectively and by making decision-making more transparent and fair.

Yet, Western experience has shown that federal systems are continuously subject to the renegotiation of the status-quo.<sup>385</sup> As Russia integrates further into the global economy, the incentives for regional governments to expand their policy authority and

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<sup>384</sup> See "Introduction," in Peter Rutland, ed., *Business and the State in Contemporary Russia* (Boulder, Colorado: Westview Press, 2001).

<sup>385</sup> Ordeshook and Shevtsova, 1997.

fiscal resources will likely increase, as has been the case in Canadian and European federal systems.<sup>386</sup> And even if the Putin regime continues to move closer toward a de-facto unitary state, the necessity of promoting salutary interregional (e.g. fiscal federal) competition to promote economic growth may dictate de facto power-sharing arrangements with regional governments, as in the case of China.<sup>387</sup>

Thus, whether Russia develops along the lines of either a semi-authoritarian model closer to the Chinese one or a western model of federal democracy, it must develop a strong national party system that would link the career ambitions of regional governors with national politicians.<sup>388</sup> The role of vertically integrating mechanisms that can bind the interests of politicians at various levels of government is essential to structuring bargaining and reciprocity. As a broad based national party, United Russia could theoretically fulfill this role. It encompasses a much broader number of regions than big business, which has much more narrow political and geographical interests. At the same time, Putin's personal attitude toward a national party system will be of key importance in its future development.<sup>389</sup> In particular, the danger exists that United Russia will either fade away after Putin leaves office (as has occurred when the chief patrons of previous "parties of power" have left office), or that it will evolve into a "top-down" mechanism dominated by federal bureaucrats, especially the statist-minded

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<sup>386</sup> Keating, 1998; Benz, 1999; Mclure, 1983.

<sup>387</sup> Li and Lan, 1999.

<sup>388</sup> Blanchard and Schleifer, 2000.

<sup>389</sup> Robert Moser, "Executive-Legislative Relations in Russia" in Barany and Moser, 2001.



*siloviki* – the “law and order” elites that have gradually come to dominate Putin’s administration.<sup>390</sup>

An important finding in regard to democratization is that the “balancing” effect of national-level businesses in Russia’s federal system has been a function of the macro-political context. During the crisis-ridden 1990s, when the “party of power” was much weaker, the expansion of national-level businesses in the periphery acted as a vital centripetal mechanism that allowed the federal center to constrain and co-opt would-be assertive regional elites, helping to stave off a slide toward de-facto confederative relations that could have threatened state breakdown. Moreover, as Putin consolidated power during his first term, regions where national-level business had established a strong presence were more compliant with federal legislation to eliminate the bilateral power-sharing treaties. The abrogation of these treaties has helped strengthen a greater number of regional executives’ stakes in the federal bargain, since they were viewed as being both opaque and unfair, and were a constant source of contention.<sup>391</sup>

However, in the context of a semi-authoritarian regime that could emerge if the Kremlin continues to centralize power – both “horizontally” and “vertically” – during Putin’s second term, big businesses could potentially play either of two political roles. The first could be a balancing force against the *siloviki* and defender of liberal interests on both federal and regional levels, especially in terms of supporting opposition parties, and championing formal institutions and legislation that limit state interventionism and

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<sup>390</sup> Reddaway, 2002.

<sup>391</sup> Only half of the regions signed bilateral power-sharing treaties with the federal center. Most importantly, the decision-making process did not take place in parliament, and many parts of the treaties violated the Russian Constitution.

strengthen property rights.<sup>392</sup> The second role, however, could be as an appendage of an assertive central state, in which case big businesses would contribute to an *imbalance* (e.g. over-centralization) of the federal system. Before these scenarios are examined in more detail, it is necessary to outline the relationship between the level of political centralization and fiscal federal performance in emerging-market countries such as Russia.

### **Toward “Market-Preserving” Federalism?**

As discussed earlier, one of the chief benefits of “market-preserving” federalism is efficiency-enhancing competition among federal subjects for labor and capital, which motivates regional governments to provide competitive policy environments for businesses and, ideally, adequate social services for the labor force. More specifically, the basic tenets of market-preserving federalism are as follows:<sup>393</sup>

1. Clear delineation of authority between various levels of government;
2. A high degree of regulatory authority of subnational governments in their jurisdictions;
3. Enforcement of rules by national authorities providing for a common market and mobility of goods and other productive factors between jurisdictions;
4. Revenue sharing and borrowing is subject to hard budget constraints; and
5. The nature of federal relations is institutionalized and not easily changed (unilaterally) by either central or regional governments.

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<sup>392</sup> Some of the same oligarchs who were linked to “crony capitalism” under Yeltsin in the 1990s have emerged as the chief defenders of liberal democracy under Putin, such as B. Berezovsky and M. Khodorkovsky.

<sup>393</sup> Gabriella Montinola, Yingyi Qian, and Barry Weingast, “Federalism, Chinese Style: the Political Basis for Economic Success in China,” *World Politics* 49 no. 1 (1995):50-81. For federalism to “work” as a political system encouraging economic efficiency and growth, the central state must be able to ensure adequate mobility of labor and capital among regions, and regulate competition (e.g. discipline rent-seeking behavior and fiscal irresponsibility).

As suggested by point three, the success of a market-preserving federal system hinges in large part on the autonomy of the central state. It must have the ability to police the behavior of both regional governments and business actors in order to prevent collusive relationships which undermine market competition and tax collection (e.g. regulatory and extractive capacity).<sup>394</sup> In the same vein, both regional governments and businesses need to have some degree of autonomy (point two), as well as certainty regarding the rules of the game in general, and their property rights in particular (point five), in order for interregional (e.g. fiscal federal) competition to be efficiency-enhancing. In an environment of arbitrary rules, incentives to maximize individual gains, which could be taken away by a predatory federal government, are weaker.<sup>395</sup>

As the Chinese case has shown, autonomy does not necessarily have to be constitutionally guaranteed, though the credibility of the center's commitment to honor intergovernmental agreements is important.<sup>396</sup> However, when the state is unable to police a common market infrastructure, assertive regionalism can lead instead to "market-distorting" federalism, which is characterized by market fragmentation and autarky.<sup>397</sup>

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<sup>394</sup> The federal center must be able to address interregional socioeconomic asymmetry, which can result in an uneven playing field for regions, as the gap between wealthy and poor regions increases, which requires strong distributive capacity.

<sup>395</sup> Weingast, 1995.

<sup>396</sup> Li and Lan, 1999.

<sup>397</sup> See Slider, 1997 and OECD, 2000 and 2003. There was no clear definition of authority (point 1) between various levels of government, and the bilateral treaties signed in the 1990s were more of a matter of political expediency than economic efficiency. There also was a lack of central control (federal regulation) over the common market (point 3), leading to a fragmented economic space and instances of regional economic separatism, as various regulatory bureaucracies were captured by regional officials. Moreover, regions did not face hard budget constraints (point 4) because of weak enforcement of borrowing limitations and the prevalence of monetary surrogates. Finally, federal relations were not institutionalized in practice (point 5). Formally, the federal center retained a high degree of control over

The theory of market preserving federalism stresses the need for a “strong state” in addition to the “strong region” of classic fiscal federal theory.

Table 6.1 demonstrates the relationship between various typologies of intergovernmental relations and progress toward “market-preserving” federalism based on the Russian case. This chart is more germane to emerging market federations, where market institutions are generally weaker.<sup>398</sup> Emerging market federations such as Russia are most effective when the politically disruptive effects of regional assertiveness are *minimized* and when the economically salutary effects of interregional competition are *maximized*, which is a point in the middle of the spectrum.<sup>399</sup> To a certain extent, a trade-off between political and economic performance is inevitable. The more the center increases its political leverage over the regions by encroaching on fiscal resources and policy competencies, the less autonomous regional governments become.

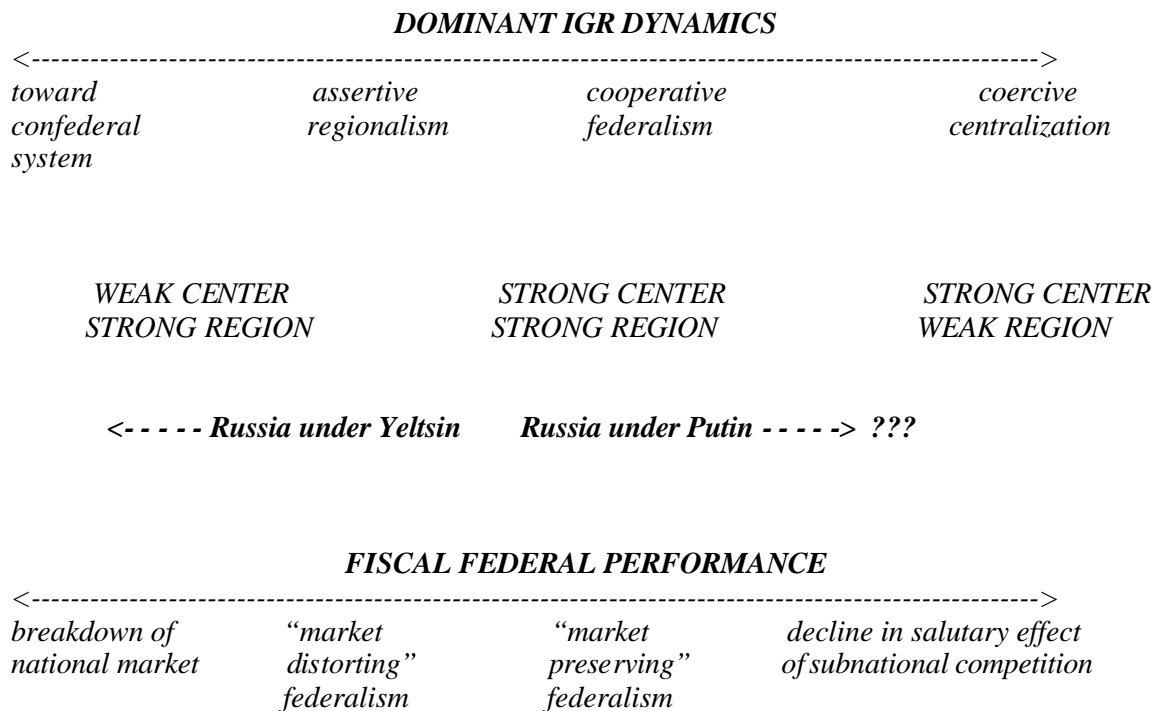
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decision-making and regions were more subject to arbitrariness of central ministries, forcing them to either assert themselves and bargain for better deals or to rely on informal fiscal practices, both of which undermined federal tax collection and created distorted economic incentives.

<sup>398</sup> The correlation between a strong state and market efficiency (e.g. market-preserving federalism) is most evident in emerging-market federations, which lack an institutional infrastructure (capital markets, bankruptcy procedures, hard-budget constraints, credit institutions, etc.) to discipline regional fiscal and economic behavior. Thus the state has to initially play a much greater role in “market-creation:” establishing and uniformly enforcing rules for horizontal competition, before it can retreat to a less active role in policing the market as in advanced federations, where the rules are self-enforcing (e.g. ‘non-efficient’ competition such as irresponsible fiscal policy, protectionism, autarky, economic separatism etc. is instantly punished by the market, and states cannot expect the federal government to bail them out). Li and Lan, 1999; Wibbles, 2000.

<sup>399</sup> Wibbles, 2000.

Figure 6.1: The “Federal Balance” in Russia



What role do state-business relations play in maintaining this balance in Russia? During the 1990s, big business played a dual role. On one hand, in the context of weak market and regulatory institutions, national-level businesses exerted a “market preserving” tendency to the extent that they integrated regional markets into the national economy. On the other hand, within the context of Russia’s “oligarchic capitalism,” the federal state was fragmented and captured by particularistic business interests, preventing it from effectively disciplining either regional governments or big business. While

serving as a mechanism of political integration, alliances between regional governments and national-level businesses have tended to crowd out competition (especially small and medium-sized enterprises) and have often relied on quasi-fiscal arrangements to the detriment of federal coffers. In the 1990s, the cash-strapped federal state was able to do little in the way of addressing mounting interregional asymmetry (the gap between the wealthy and poorer regions), while national-level businesses squirreled most of their capital abroad. The overall weakness of the federal center and ensuing fragmented national policy space led to a “market-distorting,” rather than a market-preserving, outcome for Russia's federal system.<sup>400</sup>

With the emergence of Putin, the reassertion of federal power has at first had a positive impact, moving Russia closer to the “market-preserving” end of the spectrum. As the autonomy of the federal government relative to big business and regional governments strengthened under Putin, the Kremlin has increasingly pressured big business to pay taxes and contribute more consistently to capital investment and social goals around the country.

In addition to facilitating the developmental goals of the state, corporate social responsibility also brings direct benefits for corporations that make them more willing to uphold their end of the bargain. First, the need for foreign investment (e.g. stock market) has induced changes in corporate governance and a trend toward greater transparency and attention to a corporate image. Secondly, the personal political ambitions of the enterprise or group leaders are an important motivation. As corporate leaders turn from

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<sup>400</sup> Slider, 1997.

their role as "Wild East" capitalists and increasingly eye political offices on both regional and national levels, they have striven to publicize their contribution to socioeconomic development and counter the image of a Moscow-based oligarchy plundering the periphery and siphoning assets abroad.

The overall effect of the increase in federal state autonomy and the Kremlin's emphasis on corporate social responsibility during Putin's first term was initially positive for Russia's federal system in terms of its moving Russia closer to the "strong (e.g. autonomous) federal state – strong business" balance needed for market-preserving federalism. However, as the federal center has continued to centralize power, the danger of political imbalance – this time in the form of an overbearing federal center – has reared its ugly head. The state's systematic attack on YUKOS, formerly Russia's largest privately-owned oil company (and # 4 ranked national-level business for the index period), from 2003 - 2004 has raised the specter of a "strong state – weak business" scenario, where big businesses could effectively become appendages of the state. The following section delves further into this potential danger and its implications for Russia's federal system.<sup>401</sup>

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<sup>401</sup> The imprisonment and/or forced exile of the company's major shareholders, plus the magnitude of the back tax claims brought against the company, have been widely regarded as an attack on former CEO Khodorkovsky for his political activities (active support of opposition parties, lobbying for private pipelines, etc.) and also to prevent a merger with Sibneft, which was to involve a strategic western investor.

## **Prospects for State-business and Federal Relations in Putin's Second Term**

Putin's second term could represent the end of a transition from the patterns of governance unique to the Yeltsin regime, including the model of state-business relations associated with oligarchic capitalism. It is clear that President Putin will remain the dominant political figure during his second term, and looking ahead the main question is the type of new rules of interaction between the state and big business that will be developed and enforced by the Kremlin. Two scenarios are discussed here.

The first, more positive, scenario is that lingering competition between national-level business elites and the statist-minded *siloviki* will lead to the partial institutionalization of state business relations, as the oligarchy increasingly champions formal rules to defend its interests and as Putin – mindful of the vital contribution that the oligarchs can play in assisting the state in developing the periphery – restrains the *siloviki* from pursuing a potentially costly "winner take all strategy" against the national business elites. A broader campaign to overturn privatization results would likely incite massive capital flight, while the precedent would weaken trust in property rights. This scenario could potentially involve a settlement whereby the oligarchy's property rights would be ensured through amnesty (enshrined in legislation) from further investigations related to the early years of privatization in exchange for acting as exemplary "corporate citizens" in the field of corporate social responsibility.

State-business relations would most likely take the form of state-led corporatism, with the political activity of big business curtailed in exchange for competitive favors given to "loyal" oligarchs. The key to this scenario is that the "Yukos affair" is the



exception rather than the rule, and that it represented an attempt to reinforce the rules of the game at the time when the stakes were the highest, during the federal election season. The fact that the state has vigorously pursued its case against the company after the 2003-2004 federal elections, and has planned the sale of the company's core asset, Yuganskneftgaz, suggests that the redistribution of property might have been a primary motive, which portends a more negative scenario.

Table 6.1: Scenarios for the Development of State-Business Relations

	Actors	Rules	“Market-Preserving” Federal Balance?
<b>Yeltsin Era Privatization</b>	<i>Oligarchs (1994-1998):</i> Big business fragments central state, which remains weak.	<i>Informal:</i> state capture according to oligarchic model. Equilibrium punctuated by 1998 crisis and ensuing regime change.	<i>No:</i> Weak center unable to effectively discipline regional governments and big businesses. Fragmentation of policy space and market (“market-distorting” federalism).
<b>Putin’s First Term</b>	<i>Elite Competition (1999-2003):</i> between Yeltsin-era oligarchy and its political patrons and the new regime elites ( <i>siloviki</i> ). Neither actor emerges as fully dominant.	<i>Gradual emergence of formal rules:</i> onset of uncertainty and opening of window for deeper institutionalization.	<i>Developing :</i> Partially autonomous state is able to discipline other actors. Increasing synergy with business in socioeconomic and infrastructure development in the regions.
<b>Possible Exits from Uncertainty: Putin’s Second Term, 2004?</b>	<i>Scenario #1 - State-led Corporatism:</i> neither oligarchs nor <i>siloviki</i> able to pursue “winner take all” strategy, though Kremlin remains dominant player.	<i>Formal rules</i> agreed upon in settlement brokered by Putin, further progress toward institutionalization.	<i>Deepening:</i> Central state autonomy and state-business synergy deepen to approach optimal “federal balance.” Threat of additional “Yukos affairs” remains, though, due to weak democratic constraints on central state.
	<i>Scenario #2 - Dominance of Siloviki:</i> with support of Putin, <i>siloviki</i> effect “winner take all” strategy, forcing oligarchs to flee country or sell off assets.	<i>Informal:</i> Instrumental use of state for asset-stripping, redistribution to “loyal” owners. Stable equilibrium until next regime change.	<i>Nominal:</i> Weak property rights and heavy politicization of state-business relations. National-level businesses’ role as “political sticks” offsets their role as “economic carrots” in the periphery.

This alternative outcome is that the *siloviki* gradually become the dominant actor within Putin’s entourage, and instrumentally use state capacity to overturn the results of earlier privatizations and force the remainder of the Yeltsin-era oligarchy to cash in and

flee the country. This scenario would become likely were Putin to decide that the benefits of a wide-ranging redistribution of assets were greater than the potential costs to the economy.<sup>402</sup> At the same time, the dominance of the *siloviki* would likely lead to the prevalence of informal rules, e.g. loyalty to the state and the dominant elite group as a prerequisite for domestic ownership of newly redistributed assets. This would be a step backward for any institutionalization in state-business relations due to the high degree of politicization of leadership positions in national-level businesses and, correspondingly, the decreased autonomy of economic actors. In this scenario, the Yukos affair would be part of a systematic redistribution of property (e.g. creation of a new “nomenklatura” system in industry) that began with the take-over and effective nationalization of media assets belonging to Boris Berezovsky and Vladimir Gusinsky in 2001-2003.<sup>403</sup>

If the pendulum does swing to this other extreme compared to the 1990s, an “assertive federal state – weak business” model of relations could distort the benefits of market-preserving federalism to the extent that big businesses become appendages of the state and investment and corporate restructuring decisions are increasingly politicized.<sup>404</sup> Moreover, if a redistribution of property results in greater control of Russia’s oil sector by state-owned companies, then the Kremlin’s ability to directly influence regional economies – as well as sub-federal electoral outcomes – would be strengthened even further. In short, the primary danger of this scenario is that national-level businesses’

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<sup>402</sup> Political benefits could include popular support: the oligarchy generally has a negative image among most of the population in Russia.

<sup>403</sup> “Purges” of management also took place in many state-owned companies under Putin, such as Gazprom.

<sup>404</sup> The fact that the government managed to derail the merger between Yukos and Sibneft, which would have created an oil super-major with the participation of a foreign strategic investor, reflects this trend.

role as political sticks would offset their potential role as economic carrots, to the detriment of democratic federalism and economically beneficial interregional competition.

National-level business actors have played an important political role in structuring patterns of intergovernmental relations in the Russian Federation. Throughout most of Russia's democratic transition, from the initial period of chaotic decentralization under President Yeltsin to President Putin's initial consolidation of power, they have acted as balancing mechanisms, helping to bind the Russian state in the face of weak national party penetration in the periphery. If democratic federalism is to deepen in Russia, a strong national party system should ideally play the primary role of vertical integration, while state-business relations on all levels of government should become institutionalized. Recent events, however, have suggested the possible emergence of another scenario where both big businesses and the "party of power" become instruments of more coercive recentralization, with potentially deleterious effects for fiscal federal performance. The hope remains that national-level business actors will continue to play a balancing force, for greater pluralism and, even more hopefully, for the consolidation of democracy in the years ahead.

## Appendix A: Regression, Variation 1 (1990-2002)

Standardized Coefficient, T-Value

Construction of IV (See Table 4-3)	1-a	1-b	2-a	2-b
<b>Macro-structural factors</b>				
Per Capita GDP	.203 t= 1.007	.496** t= 2.490	.088 t= .370	.135 t= .590
Agricultural Economy	-.043 t= -.323	0.38 t= .371	-.145 t= -.971	-.060 t= -.403
Far Eastern Region	.144* t= 1.719	.166** t= 2.164	.164 t= 1.641	.142 t= 1.475
<b>Fiscal Federalism</b>				
Natural Resources	.008 t= 0.70	-.016 t= -.158	.009 t= 0.67	.071 t= .550
Industrial Base	.048 t= .116	.114 t= .308	-.125 t= -.467	-.005 t= -.018
Budgetary Dependence (FFSR, 1995+)	-.161 t= -1.646	-.066 t= -.702	-.133 t= -.661	-.118 t= -.879
<b>Political Bargaining Power</b>				
Ethnic Homeland	.205* t= 1.769	.198** t= 1.995	.339*** t= 2.786	.281** t= 2.320
"Matrioshka" Region	.147 t= 1.240	.172 t= 1.623	.080 t= .593	.107 t= .825
Population Size	.135 t= .856	.151 t= 1.088	.285* t= 1.769	.217 t= 1.377
Electoral Partisanship	-.021 t= -.169	-0.25 t= -.222	.017 t= .119	.003 t= .021
Elite Continuity (1990-2001)	.237** t= 2.369	.218** t= 2.442	.266** t= 2.365	.316*** t= 2.855
Prior Assertiveness (1990-1994)	N/A	N/A	N/A	N/A
<b>Industrial Concentration</b>				
	.715** t= 2.096	.728** t= 2.389*	.442** t= 2.316	.326* t= 1.698*
<b>National-level enterprises</b>				
1. National Ratio (Aggregate)	-1.044*** t= -3.725			
a. Oil and Gas only		-1.293*** t= -4.147		
b. Machine & Metals		-.419*** t= -3.029		
2. Regional Ratio (Aggregate)			-.395** t= -2.420	
a. Oil and Gas only				-.476*** t= -2.792
b. Machine & Metals				-.248* t= -1.845*
R Square	.834	.873	.779	.805
Adjusted R Square	.763	.812	.683	.710

\*=significant at the p<0.1 level (90% confidence interval, two-tailed)

\*\*=significant at the p<0.05 (95% confidence interval, two-tailed)

\*\*\*=significant at the p<0.01 level (99% confidence interval, two-tailed)

## Appendix B: Regression, Variation 2 (1995 – 2002)

Standardized Coefficient, T-Value

Construction of IV (See Table 4-3)	1-a	1-b	2-a	2-b
<b>Macro-structural factors</b>				
Per Capita GDP	.056 t= .249	.271 t= 1.092	-.018 t= .070	.009 t= .033
Agricultural Economy	-.059 t= -.397	-.006 t= -.041	-.147 t= -.921	-.102 t= -.610
Far Eastern Region	.164* t= 1.819	.152 t= 1.594	.154 t= 1.440	.142 t= 1.318
<b>Fiscal Federalism</b>				
Natural Resources	-.112 t= -.897	-.131 t= -1.054	-.118 t= -.837	-.085 t= .583
Industrial Base	.280 t= .602	.277 t= .598	-.042 t= -.147	.019 t= .065
Budgetary Dependence (FFSR, 1995+)	-.127 t= -.859	-.040 t= -.343	-.088 t= -.586	-.090 t= -.594
<b>Political Bargaining Power</b>				
Ethnic Homeland	.306** t= 2.352	.318** t= 2.546	.433*** t= 3.288	.403*** t= 2.956
"Matrioshka" Region	.216* t= 1.722	.232* t= 1.754	.161 t= 1.116	.176 t= 1.207
Population Size	.132 t= .748	.161 t= .929	.290* t= 1.696	.505* t= 1.899
Electoral Partisanship	-.039 t= -.280	-0.40 t= -.290	-.010 t= .068	-.018 t= -.118
Elite Continuity (1990-2001)	.249** t= 2.211	.234** t= 2.107	.269** t= 2.231	.295** t= 2.378
Prior Assertiveness (1990-1994)	.135 t= .744	.129 t= .330	.194 t= .668	.188 t= .644
<b>Industrial Concentration</b>				
	.495 t= 1.290	.504 t= 1.327	.349 t= 1.708**	.288 t= 1.338
<b>National-level enterprises</b>				
1. National Ratio (Aggregate)	-.971*** t= -3.468			
a. Oil and Gas only		-1.083 t= -3.907***		
b. Machine & Metals		-.410** t= -2.409		
2. Regional Ratio (Aggregate)			-.406** t= -2.323	
a. Oil and Gas only				-.392** t= -2.340
b. Machine & Metals				-.293* t= -1.945
R Square	.791	.803	.746	.754
Adjusted R Square	.700	.709	.636	.635

\*=significant at the p<0.1 level (90% confidence interval, two-tailed)

\*\*=significant at the p<0.05 (95% confidence interval, two-tailed)

\*\*\*=significant at the p<0.01 level (99% confidence interval, two-tailed)

## Appendix C: Regression, Variation 3 (Unilateral Actions Only)

Standardized Coefficient, T-Value

Construction of IV (See Table 4-3)	1b/ 90-94	2b/ 90-94	1b/ 95-02	2b/ 95-02
<b>Macro-structural factors</b>				
Per Capita GDP	-.123 t= -.608	.024 t= -.152	-.047 t= -.205	.063 t= .265
Agricultural Economy	-.168 t= -.954	-.006 t= -.041	-.171 t= -1.131	-.313* t= -1.697
Far Eastern Region	.059 t= .528	.079 t= .719	.205* t= 1.996	.209** t= 2.004
<b>Fiscal Federalism</b>				
Natural Resources	.290** t= 2.118	.191 t= 1.333	-.065 t= -.439	-.105 t= -.691
Industrial Base	.244 t= .675	.309 t= .954	-.104 t= -.210	-.297 t= -1.005
Budgetary Dependence (FFSR, 1995+)	N/A	N/A	-.304** t= -2.550	-.227 t= -1.556
<b>Political Bargaining Power</b>				
Ethnic Homeland	.541*** t= 4.375	.521*** t= 4.327	.246* t= 2.000	.259* t= 2.082
"Matrioshka" Region	-.104 t= -.736	-.106 t= .777	.114 t= .838	.118 t= .862
Population Size	.010 t= .034	.033 t= .113	.324* t= 1.790	.403** t= 2.377
Electoral Partisanship	.032 t= .216	.025 t= .174	0.51 t= .356	-.065 t= -.448
Elite Continuity (1990-2001)	N/A	N/A	.269** t= 2.078	.250** t= 2.248
Prior Assertiveness (1990-1994)	N/A	N/A	.234* t= 1.702	.191 t= 1.339
<b>Industrial Concentration</b>				
	.359** t= 2.125	.386** t= 2.242	.015 t= 0.38	.238 t= 1.144
<b>National-level enterprises</b>				
<b>1. National Ratio (Aggregate)</b>				
a. Oil and Gas only	-0.339 t= -.842		-.334*** t= -3.379	
b. Machine & Metals	-0.81* t= -1.950		-.332** t= -2.531	
<b>2. Regional Ratio (Aggregate)</b>				
a. Oil and Gas only		-.334 t= -1.053		-.366*** t= -2.225
b. Machine & Metals		-.082 t= -1.825*		-.382*** t= -3.067
<b>R Square</b>	.732	.747	.793	.808
<b>Adjusted R Square</b>	.628	.649	.681	.704

\*=significant at the p<0.1 level (90% confidence interval, two-tailed)

\*\*=significant at the p<0.05 (95% confidence interval, two-tailed)

\*\*\*=significant at the p<0.01 level (99% confidence interval, two-tailed)

## Appendix D: Regression, Variation 4 (Bilateral Actions)

Standardized Coefficient, T-Value

Construction of IV (See Table 4-3)	1b/ all	1b/ oblasts	2b/ all	2b/ oblasts
<b>Macro-structural factors</b>				
Per Capita GDP	.470 t= 1.267	1.683* t= 2.603	.215 t=.628	1.207** t= 2.055
Agricultural Economy	-.067 t= -.322	-0.99 t= -.369	-.104 t= -.502	-.337 t= -1.224
Far Eastern Region	.221 t= 1.581	.272 t= 1.468	.164 t= 1.137	.221 t= 1.318
<b>Fiscal Federalism</b>				
Natural Resources	-.122 t= -.731	-.271 t= -1.332	-.133 t= -.697	-.248 t= -1.069
Industrial Base*	-1.070** t= -2.096	-1.634** t= -2.100	-.721 t= -1.47	1.782 t= -2.205
Budgetary Dependence (FFSR, 1995+)	-.138 t= -.887	.282 t= 1.426	.144 t= -.747	-.259 t= -1.056
<b>Political Bargaining Power</b>				
Ethnic Homeland	.481*** t= 2.767	N/A	.484** t= 2.695	N/A
"Matrioshka" Region	.319* t= 1.804	.493** t= 2.175	.257 t= 1.411	.410* t= 1.724
Population Size	.770* t= 1.960	1.242** t= 2.219	.764* t=1.937	1.387** t= 2.252
Electoral Partisanship	-.040 t= -.221	0.47 t= .202	-.046 t= -.247	.127 t= .509
Elite Continuity (1990-2001)	.184 t= 1.220	.252 t= 1.505	.226 t= 1.374	.316 t= 1.617
Prior Assertiveness (1990-1994)	.021 t=.121	-.125 t= -.652	.134 t= .773	.048 t=.252
<b>Industrial Concentration</b>				
	.987** t= 2.299	1.243** t= 2.280	.417 t= 1.483**	.503 t= 1.424
<b>National-level enterprises</b>				
<b>1. National Ratio (Aggregate)</b>				
a. Oil and Gas only	-.817* t=1.994	-1.856** t= -2.705		
b. Machine & Metals	-.312 t= -1.526	-.591* t= -1.928		
<b>2. Regional Ratio (Aggregate)</b>				
a. Oil and Gas only			-.22 t= -1.428	-.475 t= -1.498
b. Machine & Metals			-.95 t= -0.872	-.367 t= -1.335
<b>R Square</b>	.665	.527	.625	.455
<b>Adjusted R Square</b>	.486	.250	.425	.138 #

\*=significant at the p<0.1 level (90% confidence interval, two-tailed)

\*\*=significant at the p<0.05 (95% confidence interval, two-tailed)

\*\*\*=significant at the p<0.01 level (99% confidence interval, two-tailed)

# This version of the regression (2-b/ oblasts) is not significant at p<0.1.



## Appendix E: Additional Methodological Considerations

A separate series of regressions was run on the *oblasts* (non-ethnic regions) only. This controls for outlying cases; the wealthiest ethnic republics are clear outliers on the assertiveness index. Secondly, this also controls for heterogeneity. The salience of ethnicity in center-periphery relations was so strong in the early part of the 1990s that the strategic behavior of ethnic leaders has most likely reflected this huge asymmetry in bargaining power. The results for the non-ethnic regions mirror those for the entire group of wealthy regions. Most importantly, national-level enterprises retain their significance in all the variations.

Two steps were taken to guard against spurious results related to the significance and sign of the national-level business variable. First, the top five “borderline” enterprises listed in Table 4-1 – those which are just below the first echelon of enterprises in terms of their size – were individually factored in as “national-level” businesses. Adding each of these enterprises slightly reduced the model’s fit, whereas taking out individual enterprises already designated as “national-level” also reduced the model’s fit. This suggests that the operationalization of the independent variable is valid and that this is not an arbitrary effect.

In addition, a differently constructed version of the main independent variable was also tested. National-level businesses were subtracted from the wider pool of the top 200 big businesses, theoretically yielding “regional-level” businesses. When substituted for the national-level variable, the “regional-level” business variable was significant and positive, rather than negative, for both machine and metals as well as non-vertically integrated oil companies. The results for the control variables were the same in terms of sign and overall statistical significance. Thus, either subtracting national-level businesses from the wider pool of big businesses or including them as a separate variable yields a significant result, though the signs are different.

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